PRESCRIPTION FOR PUBLIC SCHOOL FINANCE REFORM IN TEXAS

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Vick Roling Hines

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INTRODUCTION

> A general diffusion of knowledge being essential to the preservation of the liberties and rights of the people, it shall be the duty of the Legislature of the State to establish and make suitable provision for the support and maintenance of an efficient system of public free schools. -- Article VII, Section 1, the Texas Constitution

> All free men, when they form a social compact, have equal rights, and no man, or set of men, is entitled to exclusive separate public emoluments, or privileges, but in consideration of public services. -- Article I, Section 3, the Texas Constitution

The framers of the Texas Constitution clearly recognized the necessity of public education in a democratic society. Further, they recognized that special privilege was incompatible with a democratic society. Despite the mandates of the Constitution, public school finance in Texas has been, and continues to be, inadequate for a large portion of the state's pupils. The methods of distributing state aid to local districts has created low tax burdens for the taxpayers of some districts and has imposed high tax burdens on others. Districts with small, inadequate property tax bases are not able to approach the levels of spending for education that the wealthier portion of the state's districts afford. The state's system of aid historically has maintained these two

injustices in clear violation of Article I, Section 3 of the state's Constitution.

In the summer of 1984, Governor Mark White called a special session of the 68th Legislature to address the problems of public education in Texas and to deal with the state's needs for additional revenue. That session followed a decade of fitful attempts at and retreats from substantive reform of the methods of public school finance. In fact, the comprehensive education reform bill that resulted from the session, House Bill 72, was similar in its intent to the comprehensive reform bill of 1975, House Bill 1126.

The finance portions of HB 72 have been the subject of controversy since the bill's inception. In January of 1985, the Legislature will be faced with the task of adjusting the hastily passed HB 72. The narrow purpose of this report is to provide a foundation for evaluating the proposed adjustments to HB 72. The larger purpose is to provide a basic understanding of the fundamentals of public school finance. The report will present a normative model against which school finance measures may be evaluated and will use the model to critique education funding measures

since 1975. From the model and the critiques, the author will present several recommendations for legislative action.

ORGANIZATION OF THE REPORT

Chapter II is an historical overview of state aid to public education in Texas. This history shows the incremental movement toward an equitable school funding system. Chapter III presents the basic concepts which apply to state aid in a bifurcated school funding system. The normative model is the subject of Chapter IV. That chapter sets out goals for a state funding system and discusses implementation of the goals. House Bill 72, the comprehensive school reform bill of 1984 is evaluated in Chapter V. Chapter VI contains a summary of the findings and recommendations for legislative action.

Chapter II

A BRIEF HISTORY OF TEXAS STATE AID TO EDUCATION

The Early Years

Texas was a frontier state. It had been a frontier since the sixteenth century, and remained so until the last quarter of the nineteenth century. When immigrants moved west of the Trinity River or out of the lower Brazos River plain they encountered a landscape out of the Late Pleistocene Age. Extensive herds of grazing animals roamed steppes and savannas, stalked by large predators and by stone-age man. Immigrants adapted to this environment by becoming horsemen and by adopting much of the culture of the aborigines. They became Texans. Formal education was not a high priority for frontiersmen living in such an environment. Nor was it vital for the Neolithic-style agriculture and horticulture that prevailed over much of the state during the decades bracketing the Civil War.[1]

The Texas Republic, possessed of abundant land and large debts, attempted to finance public education exclusively through a permanent endowment of large tracts of land. The grant consisted, initially, of 13,284 acres per county,

which the Congress of 1840 increased to 17,712 acres (three leagues and four leagues, respectively). Each county was to use its land "for the purpose of establishing a primary school or academy in said county." None did so.[2]

The end of the Mexican War and the annexation of Texas by the United States lead to the hope of security and stability which encouraged a new wave of settlement. Since public education had advanced in other states of the Union, many immigrants expected and demanded a system of public education in their new home. The Constitution of 1845, adopted prior to annexation to the United States, stated that the legislature should "establish free public schools throughout the state, and...furnish means for their support, by taxation of property."[3] Although the legislature complied with the mandate to levy the tax, no funds were disbursed to public schools.[4]

Over the next one hundred years, Texas experienced a civil war and a thirty-year-long guerrilla war on its territory, and participated in two world wars. It moved from a herding economy to an agrarian economy, then to an industrial one. These events, which had impacts on the evolution

of public education in Texas receive more complete treatment elsewhere. The general trend, however, was toward greater state support of local educational efforts.

The early years left several legacies which would prove important. After several false starts and failures, the Permanent School Fund, a trust fund consisting, originally, of land, reached significant proportions. The development of the oil industry and the discovery of oil on School Fund lands increased the revenues that the fund was capable of producing.

By the end of the Second World War, the system of education finance that was in place no longer met the needs of the developing, industrializing state. Texas had over 5,000 school districts (compared to just over 1,000 today) for a pupil population of 1.15 million.[5] Many, if not the majority of these districts were tax havens formed when groups of taxpayers organized their own districts to avoid the taxes of their old districts. Urban districts were allowed to tax more heavily than rural districts. State aid was distributed by a chaotic system of per capita distribution, categorical grants, and rural school aid. Finally, Texas still had racially segregated districts.

During the 1920s several academics had developed models of public school finance systems to meet the needs of the industrialized states. George D. Strayer and Robert M. Haig, both long active in school finance studies for various states developed the first modern school finance model for New York State in a report entitled The Financing of Education in the State of New York, published in 1923.[6] Paul R. Mort, of Columbia University emerged as a leader in the field, and continued to write through the 1930s. These three men developed the original *foundation school program* concept.[7]

THE GILMER-AIKIN ERA -- 1949-1975

In a sequence of events reminiscent of those preceding the school reform session of 1984, an attempt to raise teacher salaries resulted in a movement to reform the entire education finance system. Senator A. M. Aikin and Representative Claud Gilmer sponsored legislation which resulted in the appointment of a committee to study the public school system of Texas.[8] The Gilmer-Aikin report is entitled TO HAVE WHAT WE MUST, and provides a view into the committee's process of decisionmaking.[9]

The plan of school finance developed by Gilmer-Aikin contained both old and new elements. Nonetheless, the Gilmer-Aikin Laws moved Texas into the modern era of school finance. The older elements included the Available School Fund, an unequalized distribution of the revenues of the state's Permanent School Fund -- a trust fund. The new elements which are relevant to this discussion are the Foundation School Program and the County Economic Index. Since these concepts continue, in one form or another, to be part of the state system of school finance, they bear some brief elaboration at this point.

THE MINIMUM FOUNDATION SCHOOL PROGRAM

The Foundation School Program is a device for combining state and local support for education. Throughout the era of the Gilmer-Aikin reforms it was called the "Minimum Foundation Program." The term "minimum" reflected the principle that local districts could engage in discretionary spending above the amounts determined by the basic program and that the program was, in the words of the Committee, "the very minimum kind of education the citizens of Texas have said they want."[10] Regardless of the name, most foundation programs start with a basic cost which may be assumed to be

the basic cost of education for the average or typical pupil. The state and local shares of this cost are proportioned. The local share is based on some judgement of what is reasonable for the local district to raise from its own resources. So far, in Texas the local share requirement has been low, which has led to large state expenditures to affluent schools due to the mechanics of the Foundation Program. The amount of revenue that any school district raises above and beyond its state-determined local share of the Foundation Program cost becomes local enrichment, a subject which will be covered later. (See "Unequalized Local Enrichment" in Chapter III.)

The advantage of the foundation program concept is that it can achieve equalized spending among school districts according to criteria which are easily understood. Properly designed foundation programs also contribute to efficiency in the spending of state money since less aid goes to school districts which have adequate local revenue capacity. As this report will show, foundation programs can achieve such worthy results only under certain conditions.

The Local Fund Assignment and State Share are the divisions of the Foundation School Program entitlement (FSP)

of any particular district. The Local Fund Assignment (LFA) is an amount calculated on the basis of the district's revenue capacity. Since the Foundation Program entitlement is a fixed amount for any particular district at any particular time, the remainder left when the LFA is subtracted from the FSP is the state's share or the amount of state aid. The LFA is an important concept since it is the basis of the state aid calculation, and is subject to misconceptions and misinterpretations.

The Gilmer-Aikin Committee recommended that the Local Fund Assignment would be the revenue raised by applying a tax rate of 15 cents per $100 valuation to the taxable property of each district. On the average that gave a state/local share ratio of between 80/20 and 75/25.[11] Districts which had less than average taxable property would pay a smaller proportion, and wealthier districts would pay a larger proportion. On the surface, Gilmer-Aikin should have achieved a significant amount of equalization. In practice, the equalizing effects were offset by the small amount which the Minimum Foundation Program provided as the basic cost of education, by the size of the per capita, non-wealth-tested Available School Fund grants, by an inadequate measurement of district wealth, and by several accomodations

for wealthy districts.[12]

The state of property tax appraisal in Texas at the time the Gilmer-Aikin laws were written was chaotic. The Gilmer-Aikin Committee realized that the idea of applying a tax rate to the property value within a school district in order to calculate the LFA and State Share had no meaning in a system of locally determined percentage assessments of property. To get around this problem, the Committee settled on a complicated County Economic Index by which to determine the Local Fund Assignment. The index was meant to measure local economic activity -- not necessarily local tax capacity. It was a cumbersome device made necessary by the inadequacy of other institutional arrangements. By the late 1960s, the designers of the County Economic Index had become its worst critics. Dr. Edgar Morphet, one of the designers of the Index stated:

> The Economic Index approach to evaluating local ability offers a little better measure than sheer chance, but not much.[13]

CAUTIONS ILLUSTRATED BY THE GILMER-AIKIN LAWS

Rational systems of school funding are neither secret nor unknown. Fair and equitable school funding is a

simple process which is impeded by several methods and motives:

1. *Complexity* can hide a multitude of sins, and prevent effective oversight by the non-mathematical. The Bartlett Study, commissioned by the Connally Commission reported that, "complexity is one of the major faults of the Economic Index....Texas distributes more than $600 million in state school aid annually according to a system which almost defies comprehension."[14]

2. *Institutional arrangements* may prevent implementation of an effective, efficient finance structure. A true and effective foundation program was not possible before the state required 100% assessment of property. Percentage assessment was an institution that prevented change.

3. *Vested Interests.* Changes in funding create winners and losers. Reforms are accompanied, sometimes, by attempts to prevent any district from losing state aid regardless of need. The vested interests in this case are parents and/or taxpayers in wealthy districts. The extra state aid subsidizes lower tax rates and/or af-

fluent schools in such districts. The money to provide that benefit comes from the average and poor schools and from the state's taxpayers.

Although the Gilmer-Aikin Laws were a positive advance for a state which had not made any advances in rational or effective aid to education, it must be remembered that the major descriptions of foundation programs date from the 1920's and 1930's. By the 1930's some form of foundation program was in wide use in other states. At the same time, the work of the committee should not be discounted. Many of the committee's recommendations to improve the equity and efficiency of state aid to public education have not been implemented, despite reiteration over the years. For example, the Connally Commission observed that the Gilmer-Aikin Laws, as passed and despite the efforts of its sponsors, did not encourage consolidation of inefficient school districts.[16]

The Connally Commission Report -- 1968

The Gilmer-Aikin Laws produced improvements in school finance, but by the middle 1960s the inadequacies discussed above had become apparent. Senate Bill 4, passed by the 59th Legislature in 1965, established a Governor's

Committee on Public School Education with a broad mandate to conduct "a pervasive inquiry into every facet of Texas public elementary and secondary education."[17] Governor John Connally appointed Houston attorney Leon Jaworski to chair the committee and to produce a report by 1968.

The Connally Commission Report became a massive, seven-volume work which did, in fact, explore "every facet" of public education in Texas. After intensive study of the existing structure of school finance, the Commission made a number of recommendations which were in basic accord with the principles of school finance equity espoused by Gilmer-Aikin. The report, entitled The Challenge and The Chance, recommended:

1. An expanded foundation program that would be a more realistic reflection of true educational costs.
2. A Local Fund Assignment based on the market value of property within each school district. To provide this information, the Committee recommended that the state establish a Documentary Stamp Tax to provide assessment-sales ratio data.
3. A Local Fund Assignment of 20 cents per $100 valuation in 1969-70, rising to 30 cents by 1979-80. (This is a

large Local Fund Assignment compared to actual practice until 1984.)

4. Reduction of the Available School Fund (the non-wealth-tested part of state aid) by redirecting dedicated revenues from the ASF to the Foundation School Fund.

The report made a number of other recommendations concerning consolidation of small districts, pupil/teacher ratios, and administration, but the ones noted are those immediately relevant to the finance issue.[18]

The legislature failed to act on the Committee's recommendations.

The Rodriguez Case -- 1973

In 1972, U.S. District Count found the Texas method of distributing state aid to be unconstitutional in a case called Rodriguez v. San Antonio Independent School District. The case went to the U.S. Supreme Court on appeal. The Supreme Court reversed the earlier decision reluctantly, and called the state's method of financing education "chaotic and unjust." [19] The Court found, however, that it could not rule the system unconstitutional on the grounds sought.

House Bill 1126 -- 1975

In response to the threat of successful legal action, in 1975 the 64th Legislature passed House Bill 1126.[20] This measure made significant changes in the methods of school finance, and included many of the recommendations which the Connally Commission had made in 1968 and which the Gilmer-Aikin Committee had made in 1949. This bill represents the end of the era of the Gilmer-Aikin laws. It is not the end of the era of Gilmer and Aikin. Senator Aikin's influence, in particular, is still felt in Texas public education. The failings of the Gilmer-Aikin Laws should not reflect on Senator Aikin, however much his name is associated with them. To repeat, the laws, as they were passed, did not implement the recommendations of the Gilmer-Aikin Report. H.B.1126 made the following changes in the school finance system:

1. *Equalization Aid* provided an additional grant to schools with wealth per pupil less than 120 percent of the state average.

2. The bill renamed the Minimum Foundation School Program the *Foundation School Program.* The name change had two conflicting messages; it implied either that the pro-

gram now represented largess of funding, or that the state had finally dropped the pretense that the Minimum Foundation Program represented the minimum adequate level of funding.

3. The Local Fund Assignment was to be calculated on each district's *actual market value* of property.

4. The tax rate for the *Local Fund Assignment* was set at 30 cents per $100 valuation for 1975-76 and 35 cents thereafter.

5. Section 16.001 of the Education Code was amended to state clearly that it was now state policy that "each student...shall have access to programs and services that are appropriate to his educational needs and that are substantially equal to those available to any similar student, notwithstanding varying local economic factors."

The results of H.B.1126 were debatable. On the surface, it represented a major reform, but several studies reported that its equalizing effects were either nonexistent or ambiguous.[21]

Senate Bill 1 -- 1977

The controversy that followed H.B. 1126 resulted in attempts to "adjust" the bill in every following legislature. Senate Bill 1 in 1977 was one such adjustment.

1. The Local Fund Assignment (LFA) was reduced from 35 cents per $100 valuation to 18 cents. Reducing the LFA is a common reaction of the legislature. As this report repeatedly shows, LFA reduction is not appropriate. The reduction of the LFA caused a large reduction in the equalizing effect of the program. To offset the losses which the below-average-wealth schools would have experienced, the total appropriation for the Foundation School Program was increased. The largest part of the increase went to schools of above average wealth.
2. The scope of the Foundation School Program was increased to include special and vocational education which heretofore had been categorical grants. The state aid attributable to these programs became wealth-tested. This was an improvement over the previous practice of giving this aid as categorical grants, but the net effect of S.B. 1 was disequalizing. The reduced Local Fund Assignment probably eliminated any improvements that the larger program would have produced.

An analysis by Sunderman and Hineley showed that S.B. 1 resulted in disequalization; the wealthiest districts received larger increases in aid than the poorest districts.[22]

Senate Bill 350 -- 1979

S.B.350 repeated the trends of S.B.1. Passed in 1979, it lowered the LFA to 15 cents, with a corresponding reduction in the equalization effect of the finance formulas. The bill added two provisions to shield wealthy schools from the equalizing effects of the Foundation School Program formula:

1. *Minimum aid* was a guarantee that no district would receive less state aid per pupil than in some previous year, regardless of the district's current economic situation. Prior to the passage of H.B.72, the 1980-81 school year was the benchmark.

2. *Hold-harmless* clauses guaranteed that no district's Local Fund Assignment could exceed its previous year's Local Fund Assignment by more than 120 percent. Under this provision, a district which became wealthy, or gained a larger tax base, was protected from

corresponding reductions in state aid. The reader should remember that if a district's wealth per pupil doubles, the district can raise the same amount of money per pupil as it did before with half the tax rate. Conversely, with the same tax rate, it can raise twice as much money. Hold-harmless provisions ensure that such districts are protected against drops in state aid. The same argument applies to minimum aid.

The bill reduced the Local Fund Assignment from 18 cents to 15 cents which, again, reduced the equalizing effect of the Foundation School Program. In defense of the 66th Legislature, passage of the major property tax reform bills during that session raised serious questions about the fiscal security of the state's school districts. The ultimate impact of the agriculture productivity and homestead exemptions, as well as 100 percent appraisal of property, were unknown. The bill's education finance provisions were intended to mitigate the effects of the property tax reforms.

Senate Bill 621 -- 1979

With the passage of S.B. 621 in 1979, Texas, for the first time, had a system by which to evaluate local revenue capacity for effective and efficient allocation of

state aid. The bill reformed property tax practices, mandated 100 percent assessment, and reorganized the administration of the property tax.

House Bill 246 -- 1981

H.B.246 in 1981 had indirect implications for school funding. It mandated an expanded and uniform statewide curriculum. Schools which were not in substantial conformance faced the expense of conformance by 1985. Since the schools that were less likely to be in conformance tended to be less wealthy, H.B.246 increased the pressure on the legislature to pass further finance reforms.

House Bill 72 -- 1984

By the first session of the 68th Legislature in 1983, public awareness of the problems of public education was at a high point. There was considerable pressure to increase teachers' salaries as well. The House of Representatives refused to act without current information. In response, Governor Mark White appointed the Select Committee on Public Education (S.C.O.P.E.), chaired by Dallas businessman H. Ross Perot. The SCOPE Committee created considerable controversy by challenging many of the institu-

tions and conventions which had come to characterize public education in Texas. The finance reforms, however, were not substantially different from those recommended by the Connally Commission in 1968, although they differed in appearance since the context of education had changed.

The SCOPE recommendations, which would have produced a truly just, efficient, and effective school finance system, were compromised to produce Senate Bill 4. The House produced H.B.72 with additional compromises. The Senate-House Conference Committee produced the final version of H.B.72. H.B.72 is the subject of a later chapter, but a brief listing of its finance provisions follows:

1. The concept of equalizing school funding within the context of the Foundation Program was expanded.

2. State aid distribution was based on pupil population (average daily attendance) rather than teaching staff (personnel units).

3. The Foundation School Program was expanded to conform more closely to the true accountable costs of education, and a process was instituted to apprise the legislature of changes in accountable costs.

4. The Local Fund Assignment was calculated by a different method. Previously, the Local Fund Assignment was calculated as the amount of revenue that would be produced by a uniform tax rate on a particular district's tax base. Under H.B.72, the average district's Local Fund Assignment is set at 30 percent of its total Foundation School Program grant in the first year and 33 percent thereafter. A wealth-test formula alters this proportion for each district so that the state share is a larger proportion for poorer districts and a smaller proportion for wealthier districts. At a district wealth of 330 percent of the state average wealth, districts are no longer eligible for aid from the Foundation Program Fund in the first year. Thereafter, eligibility stops at 300 percent of the state average wealth. A transition fund protects districts above these limits from abrupt losses of aid over a period of three years.

5. The bill introduced a Price Differential Index which adjusts the per-pupil allotment of each district for uncontrollable cost factors such as highly competitive job markets which increase salary demands for qualified teachers.

Table II-1 compares the major features of the finance portion of H.B. 72 to the system which preceded it.

H.B.72 was the most thoroughgoing finance reform of the decade, and represents a potentially durable structure for further reform in school finance. The bill did not accomplish the sweeping reforms envisioned by the SCOPE Committee, nor did it reach the goals set by the Connally Committee. The remainder of this paper will deal with the the shortcomings of H.B.72 as well as its strengths.

Table II-1

Comparison of H.B. 72 With Prior System

SCHOOL FINANCE PRIOR TO H.B. 72	HOUSE BILL 72
Foundation School Program	**Foundation School Program**
* Basis for Aid Allotment: Personnel Units	* Basis for Aid Allotment: Average Daily Attendance
Adjustments to Allotment	Adjustments to Allotment
Special Pupil Populations -- extra aid for pupils with special needs.	Special Pupil Populations -- extra aid for pupils with special needs.
Special District Circumstances -- Small and sparse districts received extra aid to compensate for poor economies of scale.	Special District Circumstances Small and sparse district formulas aid districts with inefficiencies due to size. * Price Differential Index compensates districts for uncontrollable costs.
State/Local Share	State/Local Share
* The Local Fund Assignment (LFA) was 11 cents per $100 valuation applied to the district's tax base. The LFA was 11.5 percent of the FSP.	* The Local Fund Assignment (LFA) is 33 percent for the average district after 1984-85. The share for districts below average in wealth is less than 33 percent. Districts with up to 300 percent of the average wealth receive FSP aid after 1984-85.
Equalization Aid	**Equalization Aid**
Districts with less than 110 percent of state average wealth were eligible for aid. * The maximum entitlement depended on appropriation. In 1983-84, it was about $327. * Grant size depended on wealth.	Districts with less than 110 percent of the state average wealth are eligible to receive additional aid. * The maximum entitlement per pupil is 35 percent of the district's adjusted FSP allotment. * Grant size depends on local tax effort as well as wealth.
Unequalized State Aid	**Unequalized State Aid**
* Available School Fund per capita grants of about $500 were not wealth tested. * Minimum Aid guaranteed that districts would not lose aid from a base year -- most recently, 1980-81. * Hold-Harmless guaranteed that no district's LFA could esceed the previous year's by more than 120 percent.	The Equalization Transition Fund provides temporary protection to districts which lose aid due to the change in the state aid system.

* Major Differences

Sources: H.B. 72, Enrolled Version
V.T.C.A., Education Code, Sec. 16.

Endnotes

Chapter II

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6. George D. Strayer and Robert Murray Haig, The Financing of Education in the State of New York (New York: The MacMillan Company, 1924), pp. 173-176.

7. Walker, The Basics of Texas Public School Finance, pp. 12-13.

8. Ibid., pp. 5-6.

9. The Gilmer-Aikin Committee on Education, To Have What We Must (Austin, 1948).

10. Ibid., p. 11.

11. Ibid., p. 15.

12. Governor's Committee on Public School Education, The Challenge and the Chance, pp. 20-23.

13. Ibid., p. 53.

14. Ibid., p. 57.

15. Strayer and Haig, The Financing of Education in the State of New York, p. 74.

16. Governor's Committee on Public School Education, The Challenge and the Chance, p. 20.

17. Ibid., p. 1.

18. Ibid., pp. 66-68.

19. San Antonio Independent School District v. Rodriguez, 411 U.S. 959, 93 S. Ct. 1919: 1973.

20. Harold Sunderman and Reg Hinely, "Toward Equity of Educational Opportunity: A Case Study and Projection," Journal of Educational Finance 4 (Spring, 1979): 438.

21. Three viewpoints are available in the citations that follow. The interested reader will notice that the prescriptions for improved equity are similar:

Sunderman and Hinely, p. 441.

Texas Research League, "Essentials of an Efficient and Equitable Public School Finance System," TRL Analyzes (May 1977): 1-4.

Daniel Morgan, Jr. and Robert Brischetto, "Texas' New School Finance Bill: An Evaluation," Public Affairs Commentary XXI,5 (November 1975): 1-6.

22. Harold Sunderman and Reg Hinely, "Toward Equity of Educational Opportunity," pp. 441-447.

Chapter III

BASIC CONCEPTS IN SCHOOL FINANCE

This chapter will deal with the problems of a bifurcated system of school funding. The issues in question are a) the cost of a basic, quality education, b) local tax capacity, c) local tax effort, and d) the foundation school program concept. This chapter does not deal with possible solutions to the issues raised, which appear in Chapter IV.

The Texas Constitution states that "it is the duty of the legislature...to establish and make suitable provision for the support and maintenance of an efficient system of public free schools." -- Texas Constitution, Art. VII, Sec. 1. Within that mandate there are three mechanisms which the state could use:

1. The state may grant taxing authority to school districts. The Constitution does not require more than that. Provided that every district in the state had the same taxing capacity per pupil, this system would not create large differences in the capability of districts to support education.

2. The state may become the sole source of school funding and can prevent local districts from levying any tax.

3. The state may share responsibility for local school

finance with the local districts.

Texas uses the third system. The division of responsibility between the state and local districts is called a "bifurcated funding system." An important legal concept related to school finance is that school districts are the creatures of the state. The state authorizes their creation and grants them the power to tax and to incur debt -- Tx. Constitution, Art. VII, Sec. 3. The power to tax is the critical point. By granting school districts the power to tax, the state has allowed them to act in a surrogate capacity for the state. The grant of taxing power is a grant of money. The problem of equalization arises because the grants of taxing power to school districts are not equivalent. Therefore, Texas has rich and poor districts by the choice of the state.[1]

Each of the systems described above requires a different level of state responsibility. The first is a *laizez faire* approach which leaves the determination of educational needs and local tax effort more or less up to the local district. It assumes that the quality of education that a child deserves is that which the voters of his

or her district are willing and able to support. Total state funding, on the other hand, requires that the state determine the quality of education needed, calculate the cost of that education, and appropriate the necessary funds. The state can fund such a program from regular state revenues, or it can maintain a state-collected ad valorem tax that substitutes for and replaces the local property tax.

The bifurcated system requires estimates of basic program cost, also, but further requires an estimate of the revenue capacity of the local district. The reason for this may be seen in two extreme cases. A district with no property wealth would be financed completely by the state. In such a case, it would be necessary to know the appropriate level of funding. Conversely, an extremely wealthy district might be capable of meeting all of its educational needs with minimal tax effort. It is not logical that the state should subsidize education in such a district, given the fact that the state does not have an unlimited amount of money. In this case, the need is to determine a reasonable local share. In any case, it is neither logical nor efficient to reduce the ability of an average or poor district to provide an adequate education in order to subsidize education in districts with adequate resources.

The responsibility of the state is clear, not only from the mandates within the Constitution, but also from statute. The Education Code states, "each student...shall have access to programs and services that are appropriate to his or her educational needs and that are substantially equal to those available to any similar student, notwithstanding varying local economic factors."[2] The two principles that are the subject of the present discussion are that equivalent pupils shall receive equivalent educational opportunities and that local economic factors should have no bearing on a pupil's educational opportunities.

Understanding school finance requires understanding the factors which make up school funding in a bifurcated system. A discussion of the basic factors follows.

LOCAL TAX CAPACITY

The primary source of unequal educational funding is the variation in local property wealth among Texas school districts. The secondary reason is the willingness of local taxpayers to support education. The variation in wealth results in variation in tax effort and in the productivity of school district taxes. The variation in capacity makes

the *horizontal equity* of school district taxation in Texas remarkably poor. *Horizontal equity* occurs when equals are treated equally. For example, when the owners of equivalent property in two school districts pay the same amount of tax, horizontal *tax* equity exists between those two property owners. To the degree that they do not pay the same amount of tax, it does not. *Horizontal equity* can refer, also, to things other than taxes -- for example, to the educational opportunity of school children. When equivalent children receive equivalent educational oportunity, that is horizontal equity in education.[3]

The magnitude of wealth variation in Texas is worth a closer look. The wealthiest district has over 600 times the wealth per pupil of the poorest district and over 60 times the wealth per pupil of the average district.[4] Wealth variations of this magnitude have two consequences. First, little equity exists betweeen the taxpayers in different school districts. Second, the capability of districts to support adequate educational programs varies. Unless state aid compensates fully for the lack of capacity, the children of the poorer districts will receive neither adequate nor equivalent educations.

Legislation can affect tax capacity in a number of ways. By removing property from the tax roles, property tax exemptions reduce the revenue capacity of school districts. In order to recover the lost revenue, districts are forced to increase taxes on nonexempt property. The impact of exemptions may vary between districts. Agricultural land is an important component in the tax bases of some districts while residential property is more important in other districts. Within the wealth ranges in which the equalization and foundation programs operate, districts may receive more state aid as the result of relative losses of wealth. However, the mechanisms needed to prevent a tax burden shift are complex, and will not be addressed here. Suffice it to say that, if the state replaces the revenues lost to districts through property tax exemptions, demands on the state treasury increase.

LOCAL TAX EFFORT AND PRODUCTIVITY

Variations in local tax capacity relate directly to tax effort. In order to raise the same revenue per pupil as the wealthiest district, the average district would have to have a tax rate 60 times as high as the wealthiest district. Conversely, were both districts to raise some arbi-

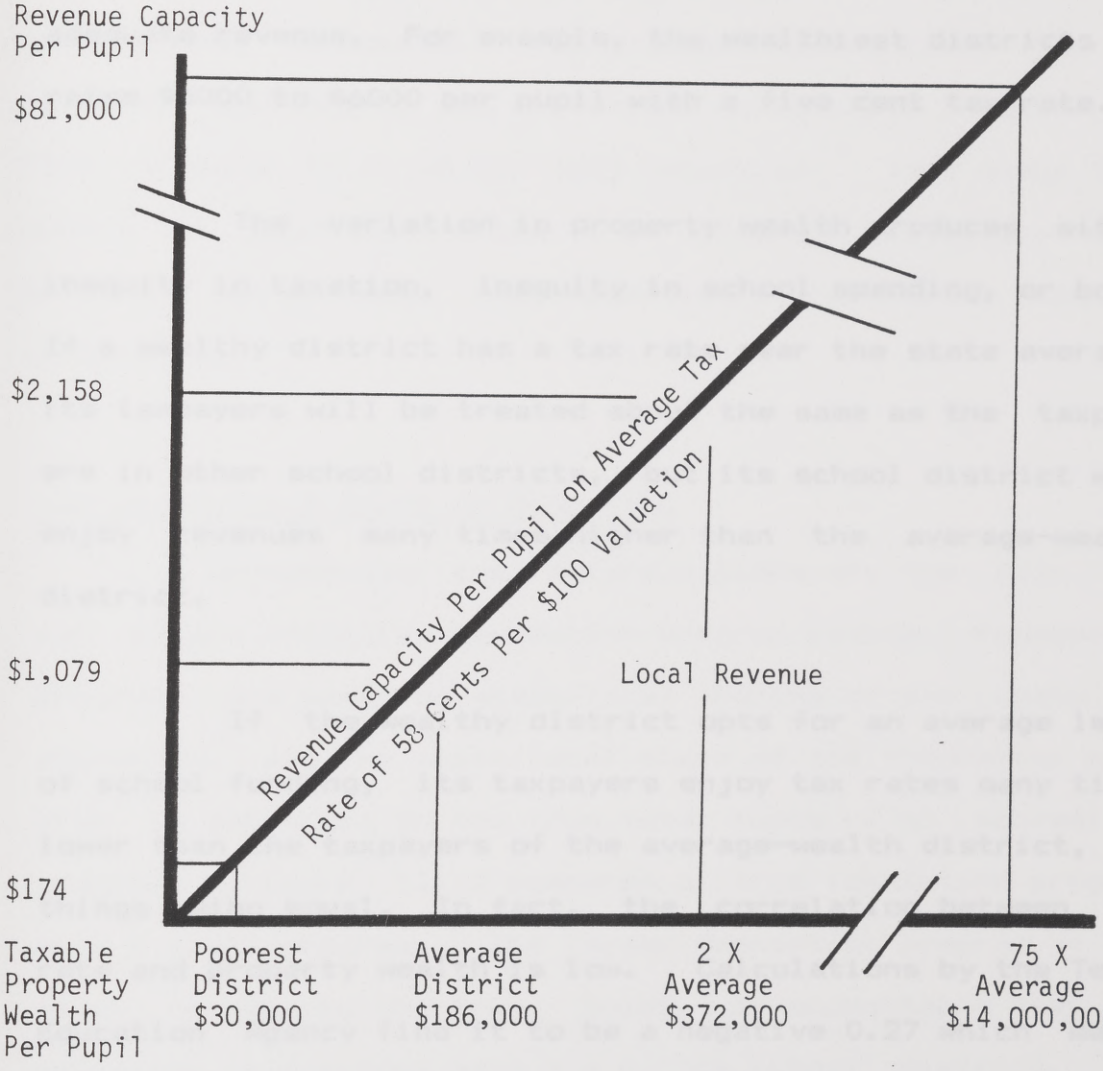
trary amount, for example, $1000 per pupil, the average district would have to have a tax rate of 43 cents per $100 valuation, but the wealthiest district would have a rate of only 7/10 of a cent per $100 valuation.[5] This variation exists in the more common wealth ranges, also. A district with three times the statewide average in property value per pupil can raise three times the revenue of the average district with the same tax rate. Conversely, it can raise the same revenue with one third the tax rate.

Figure III-1 indicates the variation in revenue capacity. The horizontal axis shows district wealth per pupil. The vertical axis shows the amount of revenue raised in dollars per pupil if all districts had a tax rate of 58 cents per $100 valuation, which is close to the current statewide average. The chart shows the one-to-one relationship between wealth and capacity. The average district has twice the capacity of the district with one-half the wealth and one-half the capacity of the district with twice the average wealth.

If the wealthiest district in the state were to levy a tax of 58 cents per $100 valuation, it would raise $81,000 per pupil. The majority of wealthy districts, how-

Figure III-1

Revenue Capacity as a Function of Property Wealth per Pupil



Revenue capacity increases as wealth increases. On any given tax rate, as property wealth doubles, revenue capacity doubles. Figure III-1 shows the revenue capacity of school districts at the average tax rate of 58 cents per $100 valuation. The wealthiest district had about 75 times the revenue capacity of the average district, and 467 times the capacity of the poorest district in 1981. The current average wealth is about $220,000. The majority of "wealthy" districts fall far below the wealthiest district, and tend to cluster between $750,000 and $3,000,000 per pupil.

Source: Texas Education Agency, "Rank Order of 1981 Index 2 Value Per ADA" (Austin: Texas Education Agency, January 18, 1983) and "Fiscal Impact Model, H.B. 72 -- Conference Committee Report"(TEA, June 28, 1984).

ever, enjoy low tax rates, since low rates will provide adequate revenue. For example, the wealthiest districts can raise $5000 to $6000 per pupil with a five cent tax rate.

The variation in property wealth produces either inequity in taxation, inequity in school spending, or both. If a wealthy district has a tax rate near the state average, its taxpayers will be treated about the same as the taxpayers in other school districts, but its school district will enjoy revenues many times higher than the average-wealth district.

If the wealthy district opts for an average level of school funding, its taxpayers enjoy tax rates many times lower than the taxpayers of the average-wealth district, all things being equal. In fact, the correlation between tax rate and property wealth is low. Calculations by the Texas Education Agency find it to be a negative 0.27 which means that there is a slight tendency for districts with large tax bases to choose low tax rates.[6] This means that many wealthy districts choose to finance their school programs well rather than to have low tax rates. Several districts levy over $9,000 per year per pupil. This does not mean that horizontal tax equity is not a problem in Texas, but that the pattern of

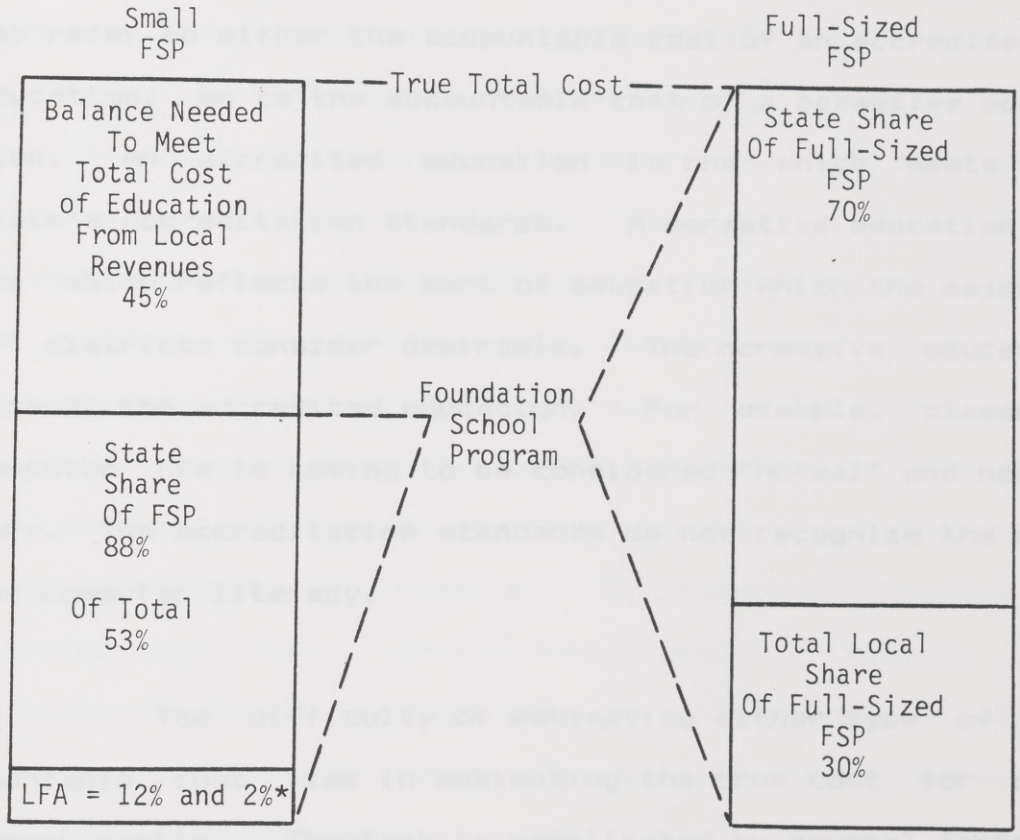
low wealth with high taxes and high wealth with low taxes is not uniform, statewide. The problem still exists. The tax rate for maintenance and operations varies from 5 cents per $100 valuation to $1.25 per $100 valuation.[7] That means that owners of equivalent property in different districts bear different tax burdens. This condition is horizontal inequity of taxation.

THE ACCOUNTABLE COSTS OF EDUCATION

Accountable cost determinations are the *sine qua non* of any effective foundation program system. Foundation programs are based on state/local sharing of the costs of education, and the state/local share of the foundation program is dependent on the true total costs of an accredited program. Figure III-2 compares a large foundation program with a small program. The larger foundation program -- one which recognizes the true, total, or accountable cost of education -- provides more aid to the school district. If the foundation program size is too small the district's total true share is large, since the district must pay for the balance of its necessary costs from its own resources.[8] Unfortunately, the task of accurately determining the true cost of education is usually ignored.

Figure III-2

The Influence of Foundation School Program Size
On True Local Share Requirements



When the Foundation School Program is smaller than the true cost of education, school districts are forced to cover the balance of the cost from local resources. The Local Fund Assignment (LFA) in the small FSP is only 12 percent of the FSP amount, but that is only 2 percent of the total cost of education for the district. The district is forced to pick up an additional 45 percent of the total cost. Under the full-sized FSP, one which covers the total cost of education, an LFA of 30 percent produces a smaller total local share.

*The LFA is 12 percent of the FSP, but 2 percent of the total cost.

Source: The proportions of the state/local share for the small FSP are the author's calculations from the Texas Research League, Benchmarks for 1984-85 School District Budgets in Texas (Austin: Texas Research League, 1984), pp. 2, 16.

The cost of education varies according to the special needs of any particular pupil. This is recognized in Section 16.001 of the Education Code. "Accountable cost" may refer to either the accountable cost of an *accredited* education, or to the accountable cost of a *normative* education. An accredited education is one which meets the state's accreditation standards. A normative education is one which reflects the sort of education which the majority of districts consider desirable. The normative education exceeds the accredited education. For example, classroom computer use is coming to be considered "normal" and necessary. The accreditation standards do not recognize the need for computer literacy.

The difficulty of estimating either type of accountable cost lies in estimating the true cost for different pupils. The task is complicated by several factors. The largest cost in education is for teacher salaries. Teacher salaries and pupil-teacher ratios vary widely among Texas school districts because of the wide differences in spending that occur. Local private-sector job markets and competition among school districts for quality teachers may increase teacher salaries in some districts but not in others, causing variation in the accountable costs that

different districts face. Extremely poor districts may push the average cost down by cutting back on programs. Small school districts have poor economies of scale, and districts in sparsely settled regions have additional support costs, so their costs are increased by a special set of factors. Finally, special interest groups, especially those involved in extracurricular activities, may drive costs up statewide by insisting on inclusion of their activities in the school program. In short, simple average costs are a poor guide to basic accountable costs. On the other hand, the cost of the accredited program alone may be too low. The accredited program does not recognize the need for classroom computer utilization. Yet classroom computers are becoming the norm. For all these reasons, the basic accountable cost should start with the cost of an accredited program, but should include the costs considered normative for a basic quality education.

Detailed discussion of the methods for determining accountable costs is beyond the scope of this paper. House Bill 72 of the 68th Legislature required the appointment of a committee to develop a methodology to determine accountable costs, but no action has been taken as of this writing. The Texas Education Agency has expressed reluctance to ful-

fill this mandate of H.B. 72.[9]

There are two methods for determining the basic accountable cost of education. The first is an econometric study to isolate the cost factors independent of local choice, local tax capacity, and local uncontrollable costs. This is similar to the method for determining the Price Differential Index (discussed later). The second method is the Basic Cost Model, which is an *a priori* accounting of the factors which make up educational costs. According to Dr. Richard Hooker, professor of school finance at the University of Houston, this is the most reliable and the simplest method.[10]

Accountable costs are a controversial political issue, since the basic accountable cost is considered to be the proper size of the basic state aid grant, or the Foundation School Program Allotment per pupil (terms which are self-explanatory, but will be defined more closely later). The accountable cost that is chosen carries several messages and has several consequences:

1. The accountable cost figure may be considered the cost of an adequate education. State policymakers can claim to have appropriated sufficient money to support public

schools without additional local taxes, and local tax opponents can argue that additional taxes are not needed, since the state has provided sufficient funds. If the accountable cost is adequate, all of this may be true, but when accountable costs are inadequate, additional money will be needed. Then the public is deceived, local tax rates may rise, or the educational opportunity available to the district's pupils will be compromised.

2. The equalizing effects of the Foundation School Program are reduced as the size of the accountable cost drops relative to true costs. This is apparent when one considers that the smaller FSP means, also, that the amount of equalized state aid becomes a smaller portion of the total cost of education in any particular district. Refer to Figure III-4. Since tax capacity varies so radically among districts, the smaller accountable cost figure means that a smaller portion of the total finance system is equalized.

Ultimately, the smaller accountable cost figure means a less-than-adequate education for the pupils living in property-poor school districts.

3. Larger than realistic accountable cost figures may lead to inefficiency. Since aid to public education is the largest single cost to state government in Texas, a little inefficiency has a large impact.

4. Larger accountable cost figures, in general, mean more cost to the state. That means higher state taxes. Given the traditional reluctance of the Texas legislature to raise taxes, the pressure to develop smaller cost figures is considerable.

5. Larger accountable costs can reduce local property taxes, since state aid can displace local revenue needs.

Regardless of the technique used to determine accountable costs, as a rule of thumb, normative costs will be larger than accredited costs. If accredited costs are used as the basis for establishing the Foundation School Program size, the final amount used should be be larger than the estimates of accredited costs indicate since the aspirations of parents and school districts will tend to encourage increases in local program size above the level determined to be reasonable by the state, unless, indeed, the state level

is obviously adequate. The discussion above used the example of classroom computer use as a cost of education which is becoming normative, although it is not recognized in the state's accreditation standards. H.B. 72 requires the Texas Education Agency to develop estimates of the accountable costs of an accredited education. The legislature should consider either extending accreditation standards to ensure that they are truly adequate, or using normative costs as the standard for the estimates of Foundation School Program size.

THE FOUNDATION PROGRAM CONCEPT

A foundation program, in general, is a structure for balancing state and local effort in systems that permit independent local taxation. There are several types of foundation programs, but all are variations on a theme.

Any equalizing foundation program balances state aid against local capacity to provide the basic program. This is the critical point. Local capacity is granted by the state. The local district is acting as a surrogate taxing authority for the state. By making the state respon-

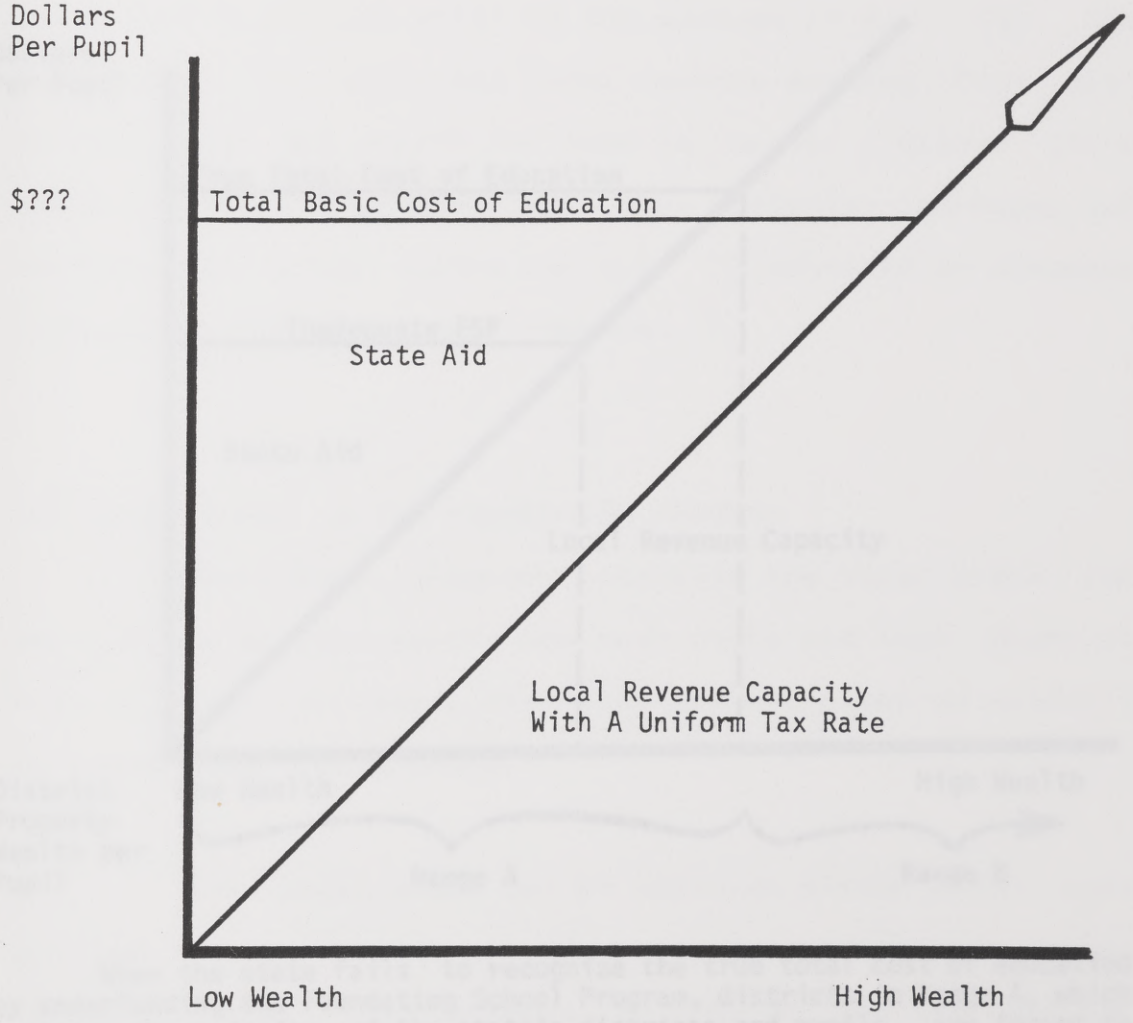
sible for education, Texas law mandates that state aid compensate for inadequate local capacity.

As Figure III-1 showed, local revenue capacity is a function of the wealth of any district. Figure III-3 shows local revenue capacity balanced by state aid. The vertical axis indicates dollars per pupil. The horizontal axis shows local taxable wealth per pupil. The diagonal line indicates how revenue capacity increases as wealth increases, as it did in Figure III-1. The *basic cost* line indicates the basic cost of education, the *accountable cost*. If a district had no taxable wealth, state aid would comprise 100 percent of the district's funding. At some point, as local wealth increases, local revenue begins to comprise 100 percent of the district's funding. Such a system meets the requirements of Texas law provided that the *basic cost* figure chosen actually accords with real costs.

Figure III-4 shows what happens when the chosen accountable cost figure is too small. Districts in Range A are unable to provide sufficient revenue to cover the basic cost of education without higher-than-average tax rates, so the system fails to comply with the equity mandates of Texas law.

Figure III-3

Balancing Local Revenue Capacity With State Aid

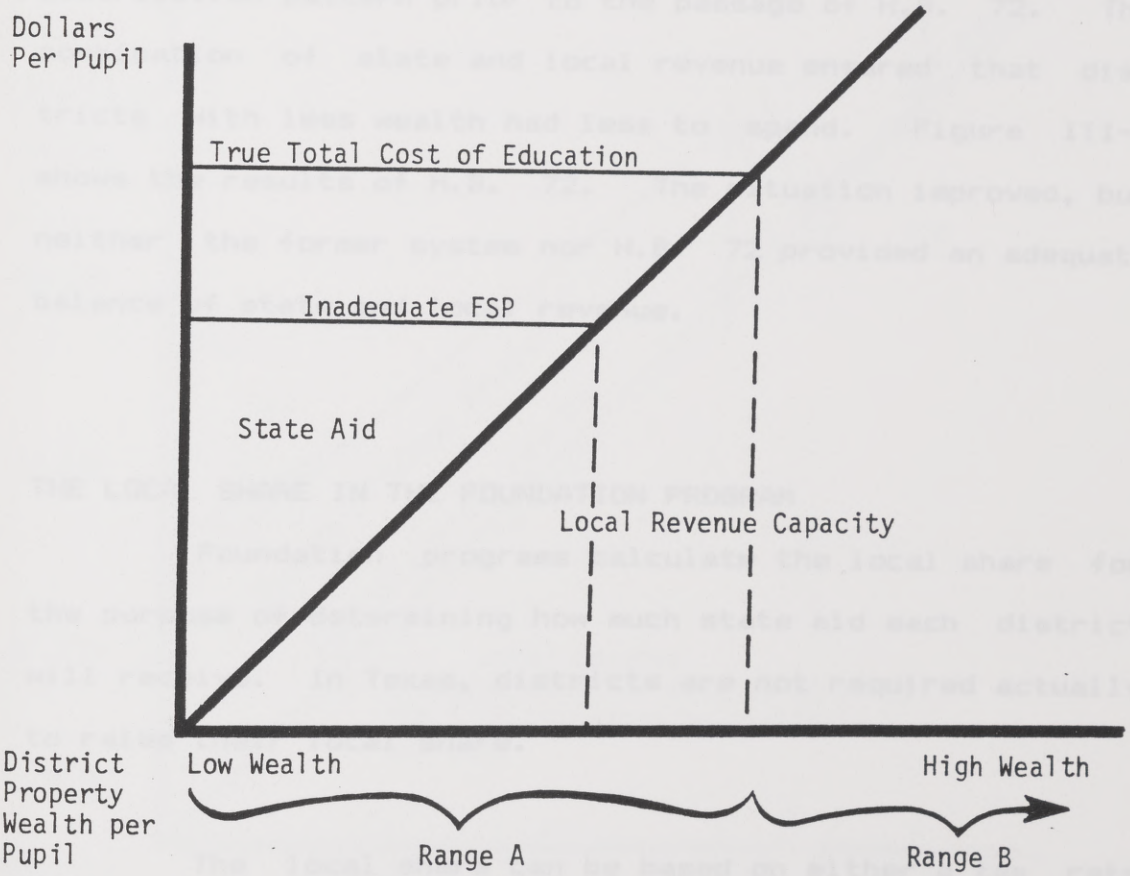


An equitable system of school finance uses state aid to balance local revenue capacity exactly. Within the range covered by state aid in the figure, all school districts would have a combination of revenues sufficient to provide a basic education, provided that the amount of state aid for the poorest district was adequate.

Source: This is a schematic representation of the revenue-balancing effect of any Foundation School Program that compensates fully for inadequate local capacity. By the author.

Figure III-4

The Result of Underfunding
The Foundation School Program



When the state fails to recognize the true total cost of education by underfunding the Foundation School Program, districts in Range A, which contains the majority of the state's districts and pupils, are forced to underfund their schools or to levy higher-than-average tax rates. Districts in Range B are able to exceed the necessary funding level with lower-than-average tax rates. Therefore, underfunding the FSP creates horizontal inequities in both taxation and education.

The figure is a simplification of the situation, since it shows only the result of underfunding a program with an equitable aid distribution, as indicated by the horizontal state aid distribution line. In reality, the distribution of state aid is not equitable. That is the subject of later discussions. The sole purpose of the figure is to show what happens when any Foundation School Program is underfunded.

Source: Schematic representation by the author.

Foundation programs can be devised which provide different distribution patterns. Figure III-5 shows the distribution pattern prior to the passage of H.B. 72. The combination of state and local revenue ensured that districts with less wealth had less to spend. Figure III-6 shows the results of H.B. 72. The situation improved, but neither the former system nor H.B. 72 provided an adequate balance of state and local revenue.

THE LOCAL SHARE IN THE FOUNDATION PROGRAM

Foundation programs calculate the local share for the purpose of determining how much state aid each district will receive. In Texas, districts are not required actually to raise their local share.

The local share can be based on either a tax rate applied to the local tax base or a percentage of the total Foundation aid. For example, in 1983-84, the tax rate for the LFA was 11 cents per $100 valuation of taxable property. A district of average wealth would have raised $186,000/100 X .11 = $204.60. Subtracting that amount from the district's Foundation School Program entitlement (which varied according to district characteristics) produced the amount of

Figure III-5

Total Revenue Distribution Prior To H.B. 72

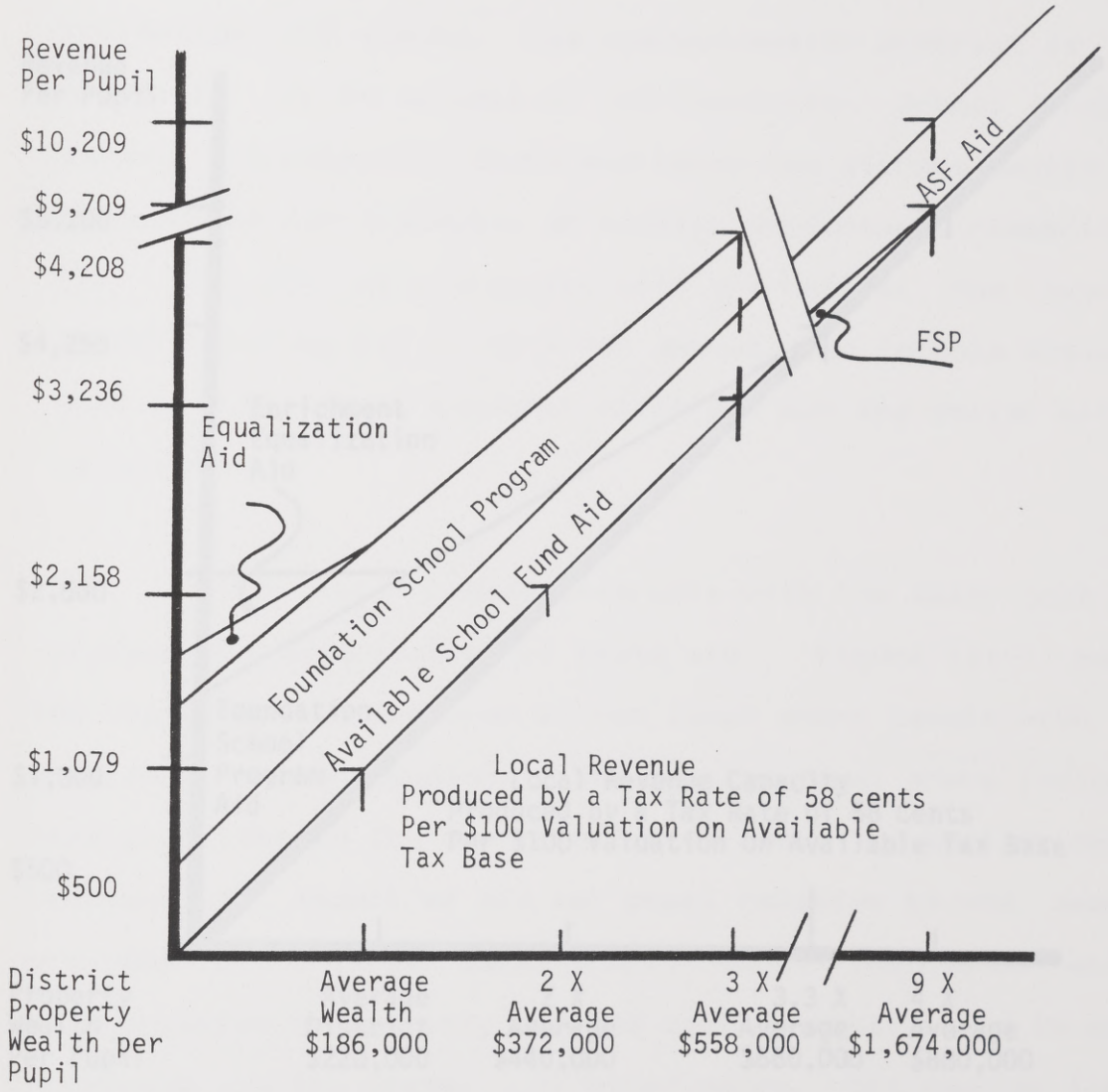
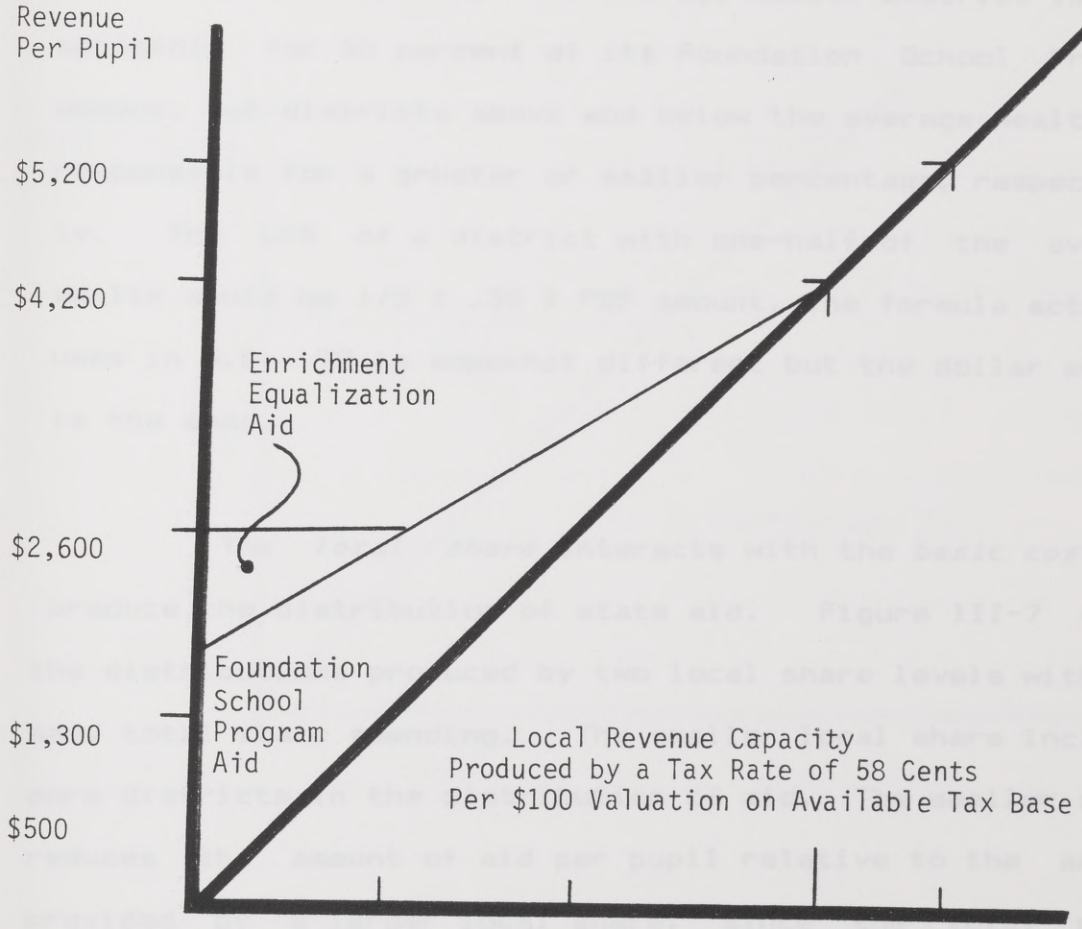


Figure III-5 is a simplified view of the distribution of aid prior to H.B. 72. FSP aid and Available School Fund money went to districts with enormous local capacity. The equalizing or revenue balancing effect of the Foundation School Program was minimal. Equalization aid was a pittance. The figure ignores minimum aid, hold-harmless provisions, textbook aid, and the state teacher retirement contribution, all of which favored the wealthier districts. It does not show how the FSP amount to which districts were entitled varied. In reality, the distribution looks like a collection of 1,069 points with a tendency to fit the lines shown.

Source: Author's calculations based on the school finance statutes prior to H.B. 72, with reference to "Fiscal Impact Model, H.B. 72 -- Committee Amendments" (Austin: Texas Education Agency, June 18, 1984), p. 2.

Figure III-6

Distribution of Revenue Under H.B. 72



Property Wealth Per Pupil	Average District $220,000	2 X Average $440,000	3.3 X Average $660,000	4 X Average $880,000

Under H.B. 72, Foundation School Program aid no longer goes to districts with over 330 percent of the average wealth per pupil. Beginning in 1985-86, aid will stop at 300 percent of the average wealth. Enrichment Equalization aid produces a flat, balanced distribution up to 110 percent of the average wealth. Thereafter, the distribution is less efficient; state aid and the state grant of revenue capacity continues to give wealthy districts the advantage over poor and average districts. This system, however, is superior in this regard to the previous system illustrated by Figure III-5.

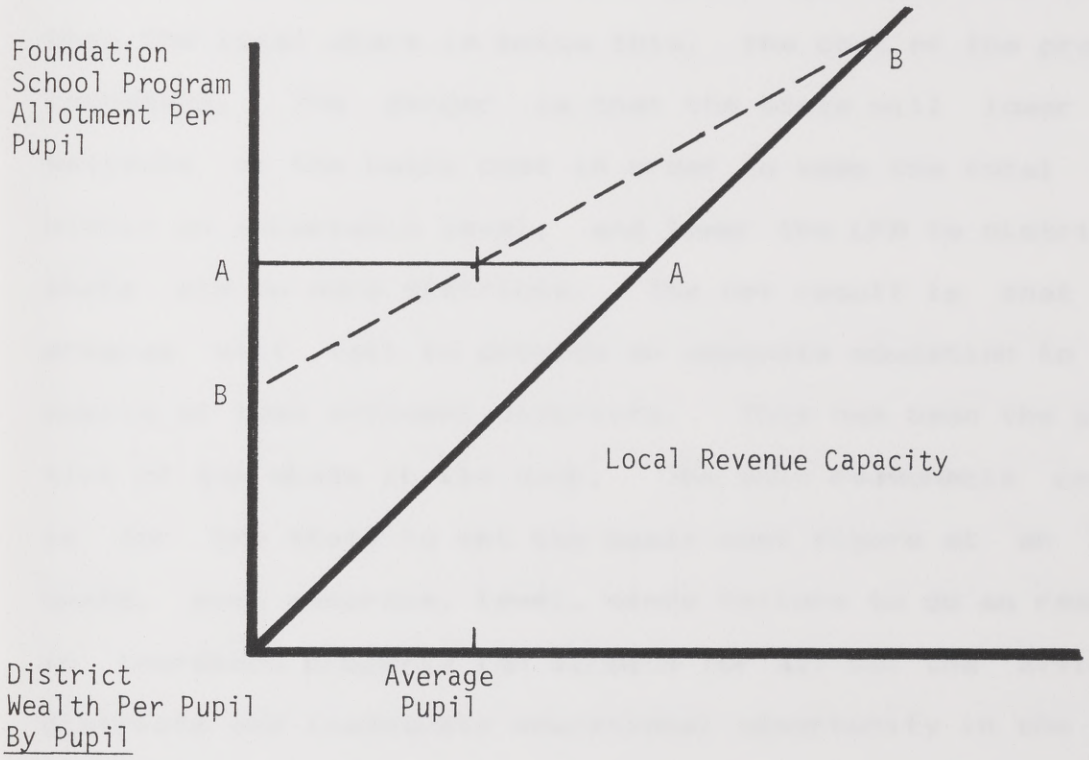
Source: "Fiscal Impact Model, H.B. 72 -- Conference Committee Report" (Austin: Texas Education Agency, June 28, 1984), p. 2.

state aid that the district would receive. Under H.B. 72, a percentage LFA system, the average-wealth district is responsible for 30 percent of its Foundation School Program amount, but districts above and below the average wealth are responsible for a greater or smaller percentage, respectively. The LFA of a district with one-half of the average wealth would be 1/2 X .30 X FSP amount. The formula actually used in H.B. 72 is somewhat different but the dollar effect is the same.

The *local share* interacts with the *basic cost* to produce the distribution of state aid. Figure III-7 shows the distributions produced by two local share levels with the same total state spending. The smaller local share includes more districts in the distribution of aid. The smaller share reduces the amount of aid per pupil relative to the amount provided by a larger local share, since the total state appropriation is limited, and the smaller local share is more expensive to the state. In other words, the smaller local share represents property tax relief for districts at the wealthy end of the spectrum, but increases the property tax requirements of districts at the less affluent end of the spectrum.

Figure III-7

The Influence of the Local Fund Assignment
On the Equity of State Aid Distribution



Given a limit on the total amount that the state is willing to appropriate for education, the size of the Local Fund Assignment is critical. It determines the amount of the FSP allotment per pupil, how many pupils and districts will receive FSP aid, and the amounts they will receive. It determines also the equity of the state aid distribution. Figure III-7 uses a different base-line, property wealth per pupil by pupil, instead of by district. Using this base, the FSP allotment for the average pupil is always the same, given that the total state appropriation to the FSP remains the same. Line A is produced by a large LFA. The large LFA results in the largest FSP allotment per pupil, but fewer pupils will reside in districts which receive aid. Line B is produced by a small LFA. The small LFA results in a small FSP allotment per pupil, since aid goes to more pupils. The larger LFA produces a more equalizing distribution of state aid, since the aid balances local revenue capacity.

Source: Author's calculations.

The local share should be an accurate reflection of the tax rate considered appropriate by the majority of school districts -- close to the average local tax rate. When the local share is below this, the cost of the program increases. The danger is that the state will lower its estimate of the basic cost in order to keep the total cost within an acceptable level, and lower the LFA to distribute state aid to more districts. The net result is that the program will fail to provide an adequate education to the pupils of less affluent districts. This has been the practice of the state in the past. The only reasonable course is for the state to set the basic cost figure at an adequate, even generous, level, since failure to do so results in increased property tax burdens for all but the affluent districts and inadequate educational opportunity in the less affluent districts.

If uniformity of taxation is a worthy goal, then the foundation program should require a "reasonable" effort that reflects what most communities have determined to be "reasonable," i.e., near the average tax rate. Any school district that cannot meet the basic cost without a higher tax effort deserves state aid. Reducing the importance of the local property tax in such a system is possible by

increasing the size of the FSP, which means increasing the accountable cost amount and, therefore, the FSP allotment per pupil. As Figure III-4 showed, increasing the FSP extends more state aid to more districts without compromising the equity of the system.

UNEQUALIZED LOCAL ENRICHMENT

Local enrichment is one of the least understood and most frequently misinterpreted concepts in public school finance. When districts raise more local money than required by their Local Fund Assignment requirement, the extra money is called "enrichment." Small local share requirements result in large amounts of enrichment. When districts, despite continuing pressure from local taxpayers, raise large amounts of enrichment, it is a signal that the estimate of the basic cost of education used in the Foundation School Program is unrealistically low. The theory of enrichment is that it represents discretionary enhancement of local school programs. Theoretically, the capability to enrich leads to the development of "lighthouse" districts characterized by innovation and excellence, which "light the educational path" for their less affluent neighbors. This belief assumes that only money allows innovation, and that poor school districts can follow the lead even though they

may not have the resources to do so. The point is, affluent districts can provide large amounts of enrichment to enhance their programs, but the less affluent cannot, and must use their "enrichment" to provide basic program. The justifications for enrichment are *after-the-fact excuses* for the results of an unfair school finance system.

If the required local share -- the Local Fund Assignment (LFA) -- is close to the total amount that districts *actually* raise, the amount of *unequalized local enrichment* decreases, and the distribution of state aid becomes more efficient. Having less enrichment does *not* mean that districts have less money. It means only that the amounts that districts raise are counted for the purpose of calculating state aid. When the local share requirement, the LFA, falls below the district's *true* local revenues, the amount of unequalized local enrichment increases, and the state aid system becomes less efficient and less fair.

FOUNDATION PROGRAMS IN GENERAL

The first equalizing foundation program was described by Strayer and Haig in 1923.[11] The core concept is that, if the state and the local school districts are to

share the cost of education, equity of taxation and education can be achieved if the local share of the basic cost of education is proportional to the revenue capacity of the local district. This model has been influential to the development of school finance plans in Texas. Strayer and Haig's model was expanded first by Paul R. Mort and later by L.D. Haskew and Edgar Morphet. Billy Walker, author of The Basics of Texas Public School Finance outlined the following principles of the foundation program as they were finally developed[12]:

1. A foundation program should ensure an adequate, minimum educational program for all children.

As this report shows, the concept of a minimum program does not address the problems in inequity in taxation and education.

2. Each local school district should be required to levy a minimum tax rate. This levy becomes the *local share* of the foundation program. The local share requirement should be low so that all districts can participate.

Texas does not require districts to levy their local share. The local share is computed in order to allow calculation of the state share. This achieves the same purpose as Strayer

and Haig's principle without the disadvantages of a low local share. In Texas terminology the local share requirement is the *Local Fund Assignment*.

3. The amount of equalization that the program provides should be limited. Districts should retain the ability to *enrich* their programs above the state minimum.

This report argues that this principle is neither rational nor productive.

4. The program should promote local initiative and efficiency.

5. The requirements and benefits of the program should apply equally to all school districts. To ensure uniformity, as much of the program as possible should be in law rather than administrative rules or at administrative discretion.

6. The foundation program should include as much of the state's total educational funding as possible. Per capita grants and categorical grants which are not contingent on district tax capacity reduce the equalizing effect of state funding.

Texas has included within the Foundation Program most of

its categorical grants. The remaining state aid which is outside the equalizing Foundation School Program are the the transition funds of H.B. 72, the state teacher retirement contribution, and textbooks.

7. The state should institute uniform property assessment, since the foundation program concept bases the local share on local tax capacity.

Failure to mandate uniform assessment practices led to the cumbersome County Economic Index of the Gilmer-Aikin Laws. When the state attempted to use market values as the gauge of revenue capacity without mandating uniform assessment (in 1975), districts lowered their assessment ratios to capture state aid. The state was forced to establish the State Property Tax Board (its current name) to oversee local practices. In 1979, the legislature mandated uniform assessment practices in Senate Bill 621.

8. The foundation program structure should promote consolidation of small, inefficient school districts where practical.

Before the Gilmer-Aikin Laws, Texas had approximately 5,000 school districts for just over one million pupils.[13] The current number stands at just over 1,000

districts for about 2.8 million pupils.[14] That number continues to include tax avoidance districts, segregation districts and small, adjacent districts separated by athletic rivalries. The push for consolidation has eased since the state has accomplished it to a large degree.

BASIC MECHANISMS FOR FOUNDATION PROGRAMS

There are five basic mechanisms under which foundation programs can operate. The earliest was per capita distribution of state aid, advocated by Culbertson in 1903.[15] Per capita distribution does not address the problem of equalization since schools receive aid regardless of their revenue capacity. The Available School Fund is an example of a residual per capita program in Texas.

The Strayer and Haig model is an example of the *unit grant* system. The unit system follows four steps:

1) The state determines the basic cost per pupil for a minimum education.

2) The state estimates the tax rate that the wealthiest district in the state would need in order to raise the basic cost.

3) All districts in the state are required to levy the minimum tax rate determined in 2.

4) The state provides each district with the difference between the basic cost and the revenue generated by the minimum tax rate on the individual district's tax base.[16]

The Strayer and Haig model has three problems. First, the tax rate needed by the wealthiest district to raise the basic cost may be so low that the minimum statewide rate is too low to be realistic. This is the case in Texas. The wealthiest district can raise $3,000 on a 2 1/2 cent tax rate. Since the average tax rate in Texas is near 58 cents, a program based on a 2 1/2 cent rate will not reflect the actual amounts raised locally for education. Second, wealthy districts have sufficient remaining capacity to reduce or eliminate any equalizing effect. This model distributes state aid to districts with generous tax bases. Given that state resources are limited, the amount of aid distributed to the less wealthy districts necessarily is reduced. Third, estimation of the basic cost is critical to the success of the program. If the legislature is not sufficiently responsive to changes in the basic costs, ap-

propriations will fall behind real-world costs.

Harlan P. Undegraff devised the *percentage equalizing plan* in 1930.[17] Percentage equalization does not use the first step recommended by Strayer and Haig. That is, there is no state estimate of basic costs. The percentage equalization steps are: 1) Each district sets its own level of spending. 2) The state pays each district a percentage of the district's spending based on the district's relative wealth.

The first objection to this form of percentage equalization is that districts can *bid up* the cost of education in anticipation of receiving state aid. Second, the model does not provide guidance as to the importance of district wealth to the percentage of the state's obligation, that is, to the equalizing effect of the program. Percentage equalization has been modified in light of these problems, and has proved to be a durable plan.

Guaranteed tax base plans are of more recent vintage. There are several versions, but the basic steps are similar to the Strayer and Haig model: 1) The state determines the basic cost. 2) The state estimates the tax rate

that the average district needs in order to cover the basic cost with standard property valuation. 3) If any district must have a tax rate above the rate required by the average district to raise the basic cost, it receives state aid to cover the difference between its revenue on its tax base at the average rate and the average district's revenue.[18]

Problems with this simplified version of the guaranteed tax base plan are: 1) It equalizes poor districts to the level of average districts and assumes that the average district's revenues are adequate. 2) The rate needed on the average district's tax base to raise the basic cost may be prohibitively high. In other words, the average district may not be able to provide a minimum quality education. 3) Wealthy districts retain the ability to enrich their programs far above the capabilities of the average and below-average districts.

Power equalizing plans are similar to guaranteed tax base plans, but apply the local tax rate to some predetermined tax base, such as the state-wide valuation of taxable property per pupil. A district's actual aid is determined by the proportion of the state's total property value held by the district and the total amount of money the

state has to spend.[19]

Power equalizing plans emphasize local tax decisions, and merely provide a mechanism by which all districts, to a point, may exercise the same amount of control over local education funding as any other district. These plans make no judgement about the basic costs of education. For that reason, power equalizing alone would not permit Texas to fulfill its constitutional and statutory mandates.

ADDITIONAL EQUALIZATION AID

Since 1975, Texas has had some form of equalization aid above the basic Foundation School Program. The theory behind additional equalization is that it gives poor school districts the opportunity to enrich their programs just as wealthy districts may enrich from their own resources.

There are several problems with the concept of additional equalization. First, it obscures the need to have an adequate Foundation School Program. As this report shows, an FSP which accounts for all of the basic costs of education will produce full equality when combined with an adequate local fund assignment. With a small FSP, poor

districts need equalization aid merely to make ends meet -- let alone to provide enrichment. Second, the equalization grants have seldom been adequate to make up for the large disparities among districts. Distribution formulas for equalization aid have assumed that only districts of below-average wealth need additional aid. That assumes that districts moderately above average do not need any aid to bring their enrichment capabilities in line with wealthier school districts. In short, equalization aid is a bone thrown to the poorer districts which does not solve the problem of wealth disparities. The solution to the equalization problem is an adequate FSP. This does not mean, however, that the state should eliminate equalization aid. Equalization is unnecessary only when the Foundation School Program is truly adequate. Whenever the legislature fails to fund the FSP adequately, equalization aid is vital to prevent poor school districts from being underfunded.

SUMMARY

Each of the foundation models presented above is the product of a particular time and place, and is appropriate to its context. Culbertson's *per capita* distribution of state aid may seem simplistic and counter-productive in

light of today's wide variations in wealth between school districts. In 1903, the tax base was primarily agricultural. Oil, industrialization, and urbanization had not yet created great wealth disparities. In that context, Culbertson's plan was practical and realistic. Each of the plans described is or was practical and realistic for its context. The purpose of this report is to describe a plan that is practical for Texas now.

Endnotes

Chapter III

1. I am particularly indebted to Craig Foster, Executive Director of the Public Education Resource Equity Center for the concept of tax capacity grants which permits realistic consideration of all of the factors which make up the school finance structure.

2. Vernon's Texas Code Annotated, Education Code, Sec. 16.001.

3. Robert Bernie and Leanna Stiefel, "Concepts of Equity and Their Relationship to State School Finance Plans," Journal of Education Finance 5 (Fall, 1979): 110-121.

4. Texas Education Agency, "Rank Order of SPTB 1981 Index-2 Values Ranked on Index-2 Value per ADA" (Austin: Texas Education Agency, January 18, 1983).

The source of the enormous wealth of some districts in the state is the value of oil and gas reserves. Unlike the practice in most other states, in Texas, localities are allowed to tax minerals in the ground, as well as the surface value of land.

5. Author's calculation from 1984 figures provided by the State Property Tax Board, Bernie Little, Information Officer. Interview, Austin, September 5, 1984).

6. Central Education Agency, A Study of School Finance (Austin: Texas Education Agency, 1983), Table V-8, p. 93.

7. Texas Research League, Benchmarks for 1984-85 School District Budgets in Texas (Austin: Texas Research League, 1984), Appendix A, Column 9, pp. A-6, A-22, A-26, A-28.

8. Arvid J. Burke, Financing Public Schools in the United States (New York: Harper and Brothers Publishers, 1954): pp. 353, 354.

9. Statement by William Kirby, Deputy Commissioner for Finance, Texas Education Agency before Legislative Education Board, November 8, 1984.

10. Interview with Richard Hooker, Professor of Education, University of Houston, Austin, Texas, November 8, 1984.

11. George D. Strayer and Robert M. Haig, The Financing of Education in the State of New York (New York: The MacMillan Company, 1924), pp. 173-176.

12. Billy D. Walker, The Basics of Texas Public School Finance, 2nd ed. (Austin: Texas Association of School Boards, 1982), pp. 12-13.

13. Governor's Committee on Public School Education, The Challenge and the Chance, Research Volume I (Austin:1968), Table XIV, p. 53.

14. Texas Education Agency, "Texas Public School Pupil Information, Regular FSP Districts, Preliminary, 1982-83," (Austin: Texas Education Agency, August 5, 1983).

15. Russel S. Harrison, Equality in Public School Finance (Lexington, Mass.: Lexington Books, 1976), p. 9.

16. Ibid., p. 10.

17. Ibid.

18. Ibid.

19. Ibid.

Chapter IV

NORMATIVE MODEL

This chapter reviews the statutory and constitutional mandates which apply to school finance in Texas, and discusses them in light of the basic principles of justice. It presents basic principles of equitable school finance derived from the statutes and the constitution. It then presents a normative model of school finance which complies, as far as practical, with the principles presented.

Utilitarian Justification for Equitable School Financing

Why should school financing be equitable? There are two answers, one utilitarian, the other normative. The utilitarian answer has several facets which appeal to simple practicality and/or self interest:

1. All citizens suffer when educational opportunity is denied any group of pupils within the state. Such pupils are less suited for professional, technical or vocational employment, and Texas' high rate of in-state migration means that inadequately educated pupils of one district will have an effect on the unemployment rates, crime, and social problems of other districts.[1] The state of Texas, as a whole, loses the contributions of potentially inventive and productive citizens.

2. An equitable system would protect school districts and their pupils from the vagaries of local economic conditions. Major industries may move or close, oil prices may fall, and today's wealthy district may be impoverished tomorrow. In the long term no school district can afford to be confident about continued local prosperity. As long as the school finance system fails to meet the needs of the poorest district, every district is in jeopardy.

3. The current system results in persons of equal property wealth bearing unequal tax burdens as the result of state policy. The state subsidizes low tax rates in wealthy districts and creates high tax rates in average and poor districts. To the extent that districts with high tax burdens tend to be poor and tend, therefore, to have less adequate schools, their residents tend to suffer an additional burden of lowered real estate values since their districts are less attractive to potential residents and businesses. To the extent that tax burdens and educational opportunity are unequal among the state's school districts, the locational choices of Texas residents and businesses are reduced. An equitable system of school finance would result in more uniform tax burdens, and would relieve the econom-

ic distortions which the current system fosters.

Normative Justification for Equitable School Financing

Any mechanism of school finance should comply with the State Constitution and Section 16.001 of the Texas Education Code. To do less is to open the state to judicial challenge. The more worthy reason to comply is that both documents are accurate expressions of fundamental principles of justice. It is fortunate that the framers of those documents possessed the depth of perception that allowed them to incorporate such basic principles into the foundations of Texas government, since challenging an unjust constitution would be legally and politically difficult.

The mandates of statutes and the Texas Constitution simplify the task of formulating a normative model for public school finance in Texas. The Constitution establishes three principles:

1) The establishment and maintenance of free public schools is the responsibility of the legislature.[2]

2) The system should be "efficient."[3]

3) No individuals or class of individuals is entitled to "exclusive separate public emoluments."[4]

The Texas Education Code expands these principles:

1) Each student "shall have access to programs and services that are appropriate to his or her educational needs..."

2) The programs and services available to any student must be "substantially equal to those available to any similar student...."

3) "Varying local economic factors" shall have no bearing on the programs and services provided to any student.[5]

These legal and constitutional principles are fundamental. They express basic ideas of justice, fairness, and practical government. They are worth a closer look.

Investing the legislature with the ultimate responsibility for education is a statement of the priority of education for the framers of the Constitution. The section begins, "The general diffusion of knowledge being *essential*

to the preservation of the liberties and rights of the people...." [author's emphasis] Yet, the writers did not go on to invest the ultimate responsibility for education in any local authority. Education was and is a statewide issue. State mandated curriculum requirements and accreditation standards are a reflection of the fact that education is an *externality*; the effects of educational practices in one district are felt in other districts, for good or ill. In a strictly utilitarian sense, that is justification for state responsibility -- local government should not control services which are important to citizens outside their jurisdictions. The issue, however, goes beyond the utilitarian.

The principle that all children in the state shall have access to substantially equivalent educational opportunities is stated negatively in the Constitution and positively in the statutes. The Constitution enjoins the granting of separate privileges to any person or group.[6] This is the basic principle of justice. As Rawls puts it:

> Each person is to have an equal right to the most extensive total system of equal basic liberties compatible with a similar system of liberty for all.[7]

When the state enhances the educational opportunity of one group of school children at the expense of another group, it is in violation of both the Constitution and the basic principle of justice. The state has done this continually in the past, and continues to do so through such mechanisms as unequal grants of tax capacity, unequalized aid, and inefficient aid distribution formulas. These actions must be seen in their true light. Since the state's resources are limited, state aid to wealthy school districts must reduce the funds available to less wealthy districts.

The issue extends to tax burdens. The state *subsidizes* lower tax rates in wealthy districts by granting them broader revenue opportunities than less affluent districts. Further, the state provides funds which displace local revenue needs and, therefore, taxes. The state actively creates inequities in taxation.

The Texas Education Code mandates that all Texas schoolchildren have equivalent educational opportunity. Another basic principle of justice is that *undeserved inequalities or accidents of birth must be compensated for.* [8] A child's residence in any particular school district (or family) is surely an accident of birth. That a child who

resides in an impoverished school district should be placed at an educational disadvantage *by the state* is clearly unjust. Conversely, it is clearly unjust for the state to enhance the educational opportunity of another child who by accident of birth resides in a wealthy school district. The principle of justice would mandate that the state compensate for the poverty of the first child's school district so that his educational opportunity is equivalent to that of the child in the wealthy district.

An extension of this principle is that the education that children receive cannot be dependent upon the willingness or unwillingness of the voters in their districts to support education. The children have no choice or control in the matter. Children should not be penalized for the shortsightedness of their communities.

The Constitution mandates an "efficient" system. Given the limitations on the resources of the state, an efficient system is one which achieves the educational goals and conforms to the basic principles with the least waste. State aid should be directed first to the points of greatest need. The state's practice of providing aid to school districts with enough wealth to spend two and three times

the average for total school district expenditures clearly violates the mandate of efficiency.

PRINCIPLES OF AN EQUITABLE SCHOOL FINANCE MODEL

The following principles derive primarily from the documents cited and are characteristic, in any case, of any equitable system of state school aid. Additional comments are provided when the derivation is not clear, has not been discussed before, or is independent of the basic principles or the documents.

1) *...each student enrolled in the public school system shall have access to programs and services that are ...substantially equal to those available to any similar student....* -- Texas Education Code, Section 16.001; Texas Constitution, Art. 1, Sec. 3.

2) *...each student...shall have access to programs and services that are appropriate to his or her educational needs....*-- Texas Education Code, Section 16.001

Since the state has the primary responsibility for education, it is the responsibility of the state to determine the appropriate level of education, and to provide it.

3) *The adequacy and appropriateness of the education provided cannot depend on local economic factors.* -- Texas Constitution Art. 1, Sec. 3; Texas Education Code, Section 16.001

This principle is the core of any just state aid program. It mandates an equalizing state aid formula. To understand this logic, it is necessary to understand that local taxing authority is granted by the state. -- Texas Constitution, Art. 7, Sec. 3. The size of grants to individual school districts varies since local tax capacity varies. If the state chooses to provide different grants of revenue capacity, it must compensate for the differences among those grants through other grants.

4) *The adequacy and appropriateness of education should not depend on the willingness of the voters in the local school district to support taxes.*

In this regard, the state should serve in a child-protective capacity. There are two ways in which state aid systems can violate this principle. a) Aid formulas which reward local effort and penalize districts which do not

expend the required effort punish the *children*, rather than the unwilling taxpayers. b) Any aid system that does not require a minimum local effort allows the local share of school funding to be inadequate. This applies to any system in which the state shares funding responsibility with local districts.

5) *The state should not use aid as an incentive for districts to implement policy.*

To withhold aid as a penalty for non-compliance is to penalize schoolchildren. On the other hand, the no-lose technique of granting aid to any district which complies with a particular policy rewards districts which would comply regardless. That is, the technique is inefficient. Further, it is usually the wealthier districts which are in compliance or which can achieve compliance more easily. Therefore, incentive schemes tend to work counter to equalization. The state has control options available to enforce compliance, and should use them instead of monetary incentives.

6) *The aid system should allow the state to reduce its reliance on the local property tax, and to shift to*

more equitable, statewide tax bases.

The local property tax is the source of the problems of inequity in school finance. Total replacement of the local property tax for education would cost at least $3.2 billion.[9] Replacing a revenue source of that size may not be practical at this time, but there are equitable solutions which can reduce the importance of the property tax in school funding.

7) *State aid should account for the two types of basic cost variations in education: the special needs of special populations of pupils and cost factors related to size and location of school districts.*

Equivalent educational opportunity does not mean that an equal amount of money should be spent on every pupil. Special pupils have special educational needs and higher costs. Special populations include special education students, non-English speaking pupils and culturally handicapped students. The proportions of special populations vary among school districts. The aid system should take this variation into account.

The other cost factors include locational factors and economies of scale. Districts in competitive labor markets must pay higher salaries to maintain quality teaching staffs. Schools located in sparsely populated regions have costs associated with their isolation and with economies of scale. Small schools are more expensive to operate than large ones.[10] When the only option is to transport pupils for unreasonable distances, aid to small schools in sparsely settled regions is appropriate. See (8).

8) *The state should not permit the continuance of school districts below a reasonable size when options for consolidation exist.*

Texas has reduced the number of school districts from 5,000 to 1,000 over the past 34 years. The state continues, however, to subsidize the continuation of tax havens, segregation havens and sports rivalries.

The aid system is not an appropriate mechanism for consolidation since any aid penalty falls on the pupils. School districts are the creatures of the state, and exist with the state's permission. The appropriate solution is legal, not economic.[11]

9) *The aid system should include classroom construction aid within an equalizing system of state aid.*

There is no equity in classroom construction in Texas since Texas has no construction aid system to balance the wide variations in local tax capacity.[12] Poor school districts are forced to reduce current service levels in order to provide basic facilities. A system to meet the most pressing classroom construction needs would help relieve districts of the burden of choosing between adequate shelter and adequate teachers.

10) *The total system for state aid must be simple to understand.*

Complicated systems give control and power to the few who understand them. An essential of democracy is that issues which affect the public be accessable to the public. Complicated school finance systems are not accessible to legislators or the general public. This hampers democratic decisionmaking, and increases the potential for abuse.

11) *When possible, the system should be capable of being*

put in place through incremental adjustments to the existing system.

The incremental approach prevents the wholesale disruption and confusion that results from massive reform efforts. Provided that the state has a workable system of school finance, it should be used.

12) *The system should be sufficiently flexible that minor adjustments can keep it in conformance with the basic principles, as well as the state constitution and statutes.*

Texas now has a system which meets the basic requirements for the implementation of an equitable school finance plan. The full assessment of property mandated by S.B. 621 makes accurate allocation of state aid possible. The state and local school district administrators are experienced in the foundation system of state aid. Texas has over thirty years' experience with equalizing aid formulas. Finally, H.B. 72 of the Special Session of the 68th Legislature provides a basic structure for further reforms.

The next question is how to construct a model which

complies with the principles just described. The model described here will comply with the principle of incremental change since the structure of school funding in Texas is fundamentally sound.

DETAILS OF THE MODEL

Texas' current foundation school program is a *unit cost model* -- similar to the foundation program described by Strayer and Haig. The advantages of the unit cost approach include: 1. conformance with the constitutional mandate of legislative responsibility; 2. greater efficiency and economy; 3. effective control of costs; 4. consistency with the current system. The normative model presented here is a unit cost system. The normative model consists of the following components:

1) The *Basic Allotment* is the basic cost per Average Daily Attendance. The basic allotment must be adjusted for special populations and special district characteristics to produce each district's FSP entitlement.

2) The *Local Share* is based on a state/local share ratio. The local share of the ratio is derived from and equivalent to the average local tax rate. The state share is the balance derived by subtracting the local share from the Foundation School Program entitlement.

3) *Classroom construction aid* brings the final major portion of school finance into the equalized system. It would provide need-based aid on an equalized formula based on classroom unit costs.

4) *Supplementary Equalization Aid* identical to the current *enrichment equalization aid* is necessary to ensure that poor school districts do not suffer when the state fails to fund the basic Foundation School Program adequately.

Although the details of these components would be more complex in practice, an equitable system of school finance does not require great complexity. These four components describe a complete and relatively equitable system that is compatible with current practice. The discussion that follows deals with the details of the four components. Figure IV-1 illustrates the model.

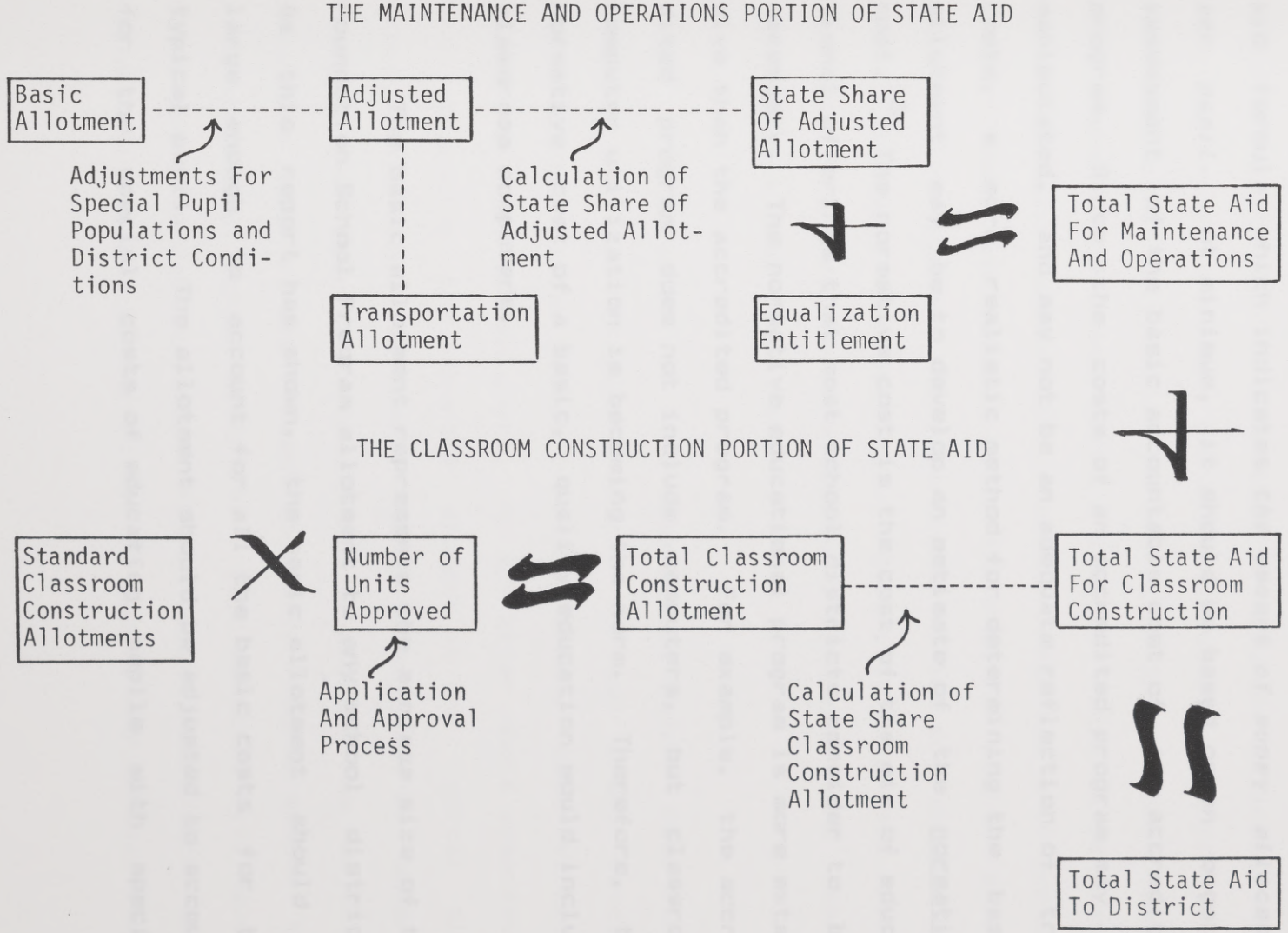


Figure IV-1: The State Aid System Under the Normative Model

BASIC ALLOTMENT

The basic allotment is the figure used in the basic aid formula which indicates *the amount of money allocated per pupil*. At minimum, it should be based on an ongoing assessment of the basic accountable cost of an accredited program. Since the costs of an accredited program may be manipulated, and may not be an adequate reflection of true costs, a more realistic method for determining the basic allotment may be to develop an estimate of the normative cost.[13] The normative cost is the cost of the mix of educational offerings that most school districts consider to be necessary. The normative educational program is more extensive than the accredited program. For example, the accredited program does not include computers, but classroom computer utilization is becoming the norm. Therefore, the normative cost of a basic, quality education would include classroom computers.

The basic allotment represents the *minimum* size of the Foundation School Program allotment to any school district. As this report has shown, the basic allotment should be large enough to account for all the basic costs for the typical pupil. The allotment should be adjusted to account for the special costs of educating pupils with special

needs. The *units* in this unit cost system are the pupils, or more precisely, the pupils in Average Daily Attendance. Since the major cost of education is teacher salaries, the cost per pupil reflects the student/teacher ratio. Unit cost models may be based on *personnel units*. In that case, the number of personnel units a district receives is based on the student/teacher ratio, also. Personnel unit systems benefit wealthier schools since their extra wealth allows them to hire teachers who rate higher in the pay scale, and the system pays them for that. Districts with less wealth are unable to hire the more expensive teachers, and therefore receive less state aid.

Calculation of the basic cost should take into account the mix of pupils in the various grade levels, pupil-teacher ratios mandated by the state, administrative costs, transportation costs, and any other costs associated with educating the "average" student in the typical district. The basic allotment should be adjusted by several factors for special circumstances to produce the *adjusted allotment* which is the Foundation School Program amount for each individual school district. Each district will have a different Foundation School Program amount since each district will have a different mix of pupils and special local

circumstances. This is in accord with the mandate of the Texas Education Code, Sec. 16.001 that each child shall have an equivalent educational opportunity. Transportation costs are a special case since mileage requirements vary among districts. This report does not address the calculation of transportation aid, nor does it evaluate the state transportation aid system. Regardless of the calculations used to determine a district's individual transportation costs, those costs should be included in the state aid formula so that state transportation aid is equalized as are the other forms of state aid.

Special Population Adjustments. A part of cost accounting is development of cost figures for specific pupil populations such as bilingual and disadvantaged pupils. This should be part of the ongoing assessment, since the costs associated with special populations may change at different rates. Special population adjustments are an overlay on top of the basic accountable costs, since the basic accountable costs are estimates based on the mix of "regular" pupils.

Price Differential Index. Any particular district's costs are influenced by factors that are beyond the

district's control. For example, if a district is in competition with a high-paying professional labor market, it will have to pay more for teachers or hire teachers who cannot compete in the market. The price differential index is an adjustment that accounts for costs that are beyond any particular district's control.

The PDI is mentioned here because it is a component of H.B. 72 and has theoretical validity. In theory, it costs more to provide a pupil in a high-cost district the same *level of education* as a pupil in a low-cost district. The PDI complies with Section 16.001 of the Education Code by adjusting for local economic factors that influence the quality of education. For practical reasons, this report argues against the immediate implementation of a PDI. The PDI is developed through application of a complex econometric model. That does not mean that the econometric model is necessarily objective. The variables selected for inclusion in the model are subject to manipulation for the benefit of selected groups of schools. Since the model is not accessible to a layman's understanding, it invites abuse. The need for simplicity indicates that adjustments for locational factors should be delayed until thoroughgoing assessment is possible. A PDI should not be implemented if it

becomes a political bargaining issue in Texas as it has in the other states that have implemented it.[14]

Small School and Sparsity Adjustments. Small schools have higher per-pupil costs because of poor economies of scale. Schools located in sparsely settled regions of the state have little opportunity for consolidation. Frequently, they are small districts due to the sparsity of settlement, and have special costs associated with their isolation. A sparsity adjustment is not a small school adjustment. It allows a larger allocation for schools that have special costs associated with their location in sparsely populated areas. There is a dilemma in providing special adjustments for small districts that do not qualify as sparsely settled, since such districts tend to be tax and segregation havens. On the other hand, failure to provide additional money to small schools, regardless of their reasons for existence, penalizes the pupils of those districts. According to the principle that the state should not use economic sanctions to enforce conformance with policy, small schools should receive adjustments. This should be accompanied, however, by legal action to force consolidation.

A GRAPHIC REVIEW OF THE MECHANICS OF THE FSP

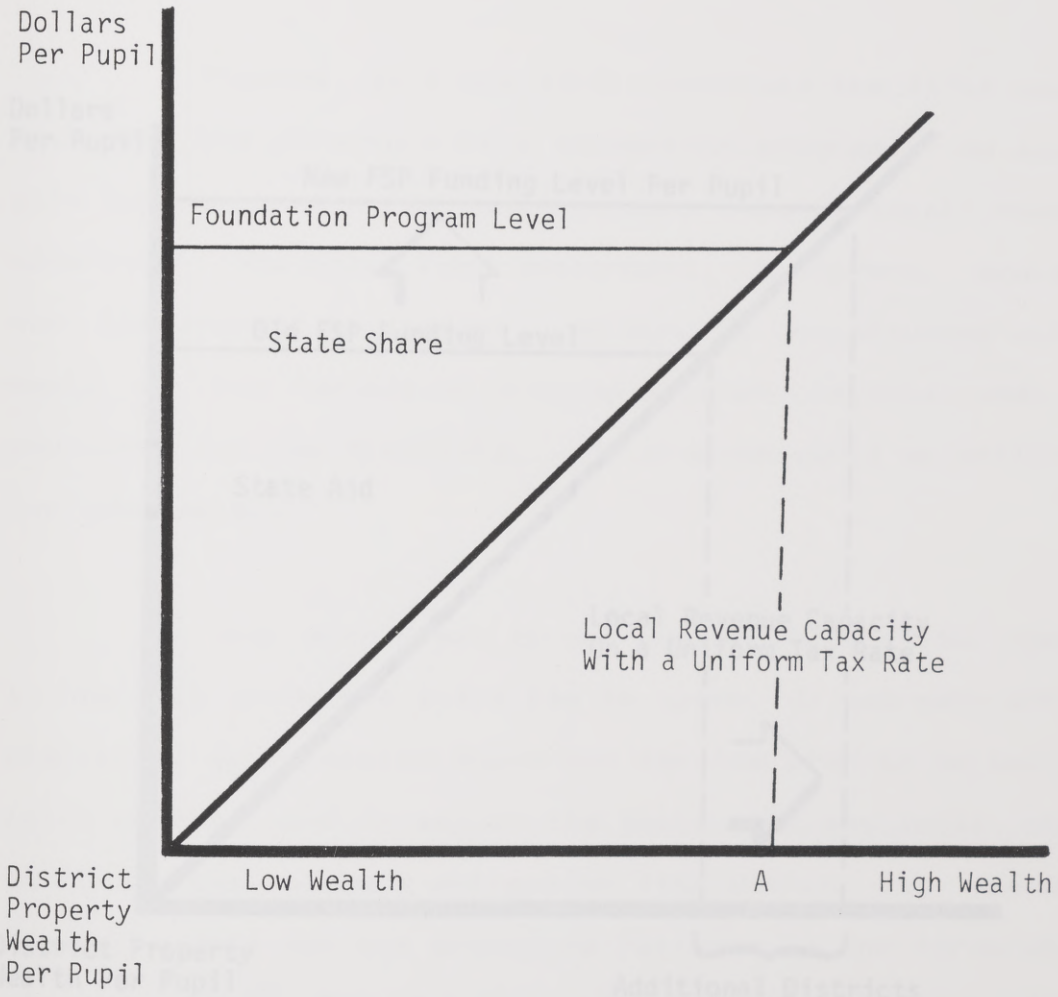
There are three ways to determine the local share and allotment size for an efficient foundation program.

Before exploring that, a short review of the mechanics of foundation programs is in order. Figure IV-2 shows revenue capacity per student as school district wealth increases against an overlay of state aid granted on a plan that balances revenue capacity. State aid exactly compensates for inadequate local revenue capacity up to point A. Above point A, district revenue capacity exceeds the size of the basic program, and districts above point A can enrich above the basic program with lower than average tax rates. As long as the Foundation School Program actually covers the cost of education, then the districts below point A can provide an adequate education.

Figure IV-3 shows that when the FSP funding level per pupil increases, the equalized region increases. The FSP level is the adjusted allotment of the FSP which should reflect the true, accountable costs that districts bear. The larger FSP allotment reflects a higher basic cost figure -- which better represents the true costs. The larger amount increases the number of districts that receive state

Figure IV-2

Balancing Local Revenue Capacity With State Aid

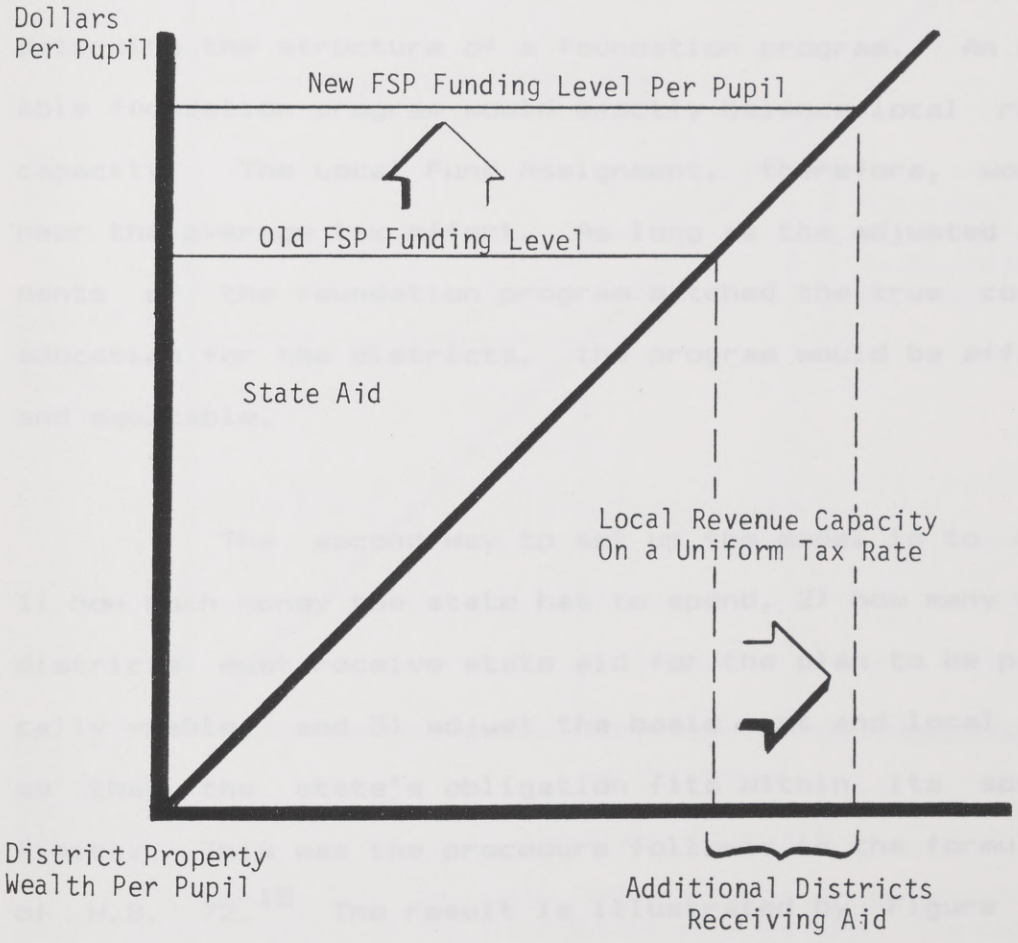


The figure shows local revenue capacity balanced by state aid. To the left of point A, state aid exactly balances local capacity on a uniform tax rate. All districts in that range have the same total revenues, although the proportion of state to local revenue varies. To the right of point A, districts receive no state aid. If these districts levy the same tax rate as the districts below point A, they can produce more revenue than districts below point A receive from the combination of state and local sources. If they choose, the districts above point A can have the same revenues with lower tax rates than districts below point A.

Source: Author's calculations from concept developed by Craig Foster, Director, The Public Education Resource Equity Center, Austin.

Figure IV-3

The Effect of the Foundation School Program Funding Level
On the Number of Districts Receiving Aid



When the amount of aid per pupil provided by the Foundation School Program increases, the number of districts that qualify for aid increases, since the revenue capacity needed to match the FSP amount is larger than before.

Source: Author's calculations

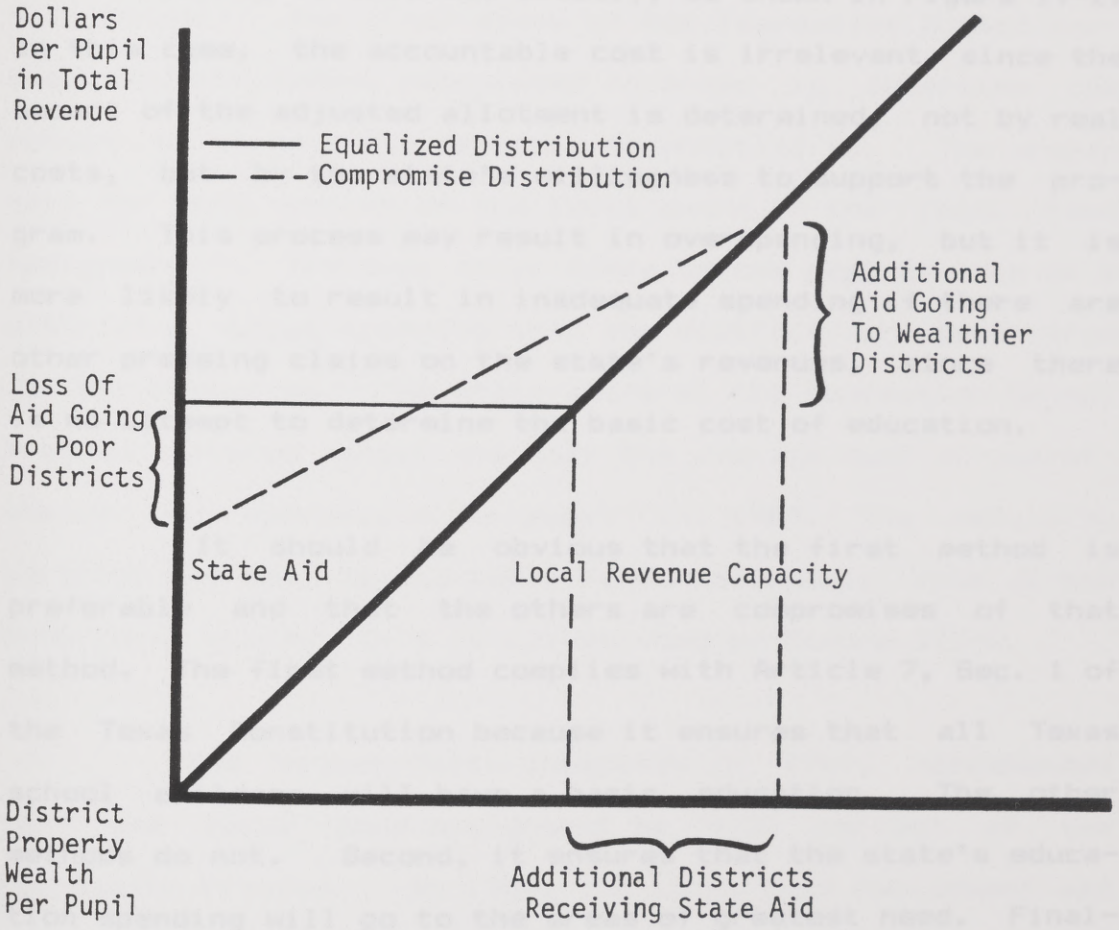
aid. This is logical, since fewer districts can support the larger program with an average tax rate.

Figures IV-2 and IV-3 illustrate the first way to determine the structure of a foundation program. An equitable foundation program would exactly balance local revenue capacity. The Local Fund Assignment, therefore, would be near the average tax effort. As long as the adjusted allotments of the foundation program matched the true cost of education for the districts, the program would be efficient and equitable.

The second way to set up the model is to decide 1) how much money the state has to spend, 2) how many school districts must receive state aid for the plan to be politically viable, and 3) adjust the basic cost and local share so that the state's obligation fits within its spending limits. This was the procedure followed in the formulation of H.B. 72.[15] The result is illustrated by Figure IV-4. The total revenue available to less affluent districts is less than that available to wealthier districts that, nevertheless, receive state aid.

Figure IV-4

Increasing the Number of Recipient Districts
Without Increasing the State's Expenditures



This figure is a schematic representation of the result of including more districts in the distribution of state aid. The compromise distribution includes districts at the wealthier end of the scale by reducing the amount of aid to the poorer districts. If the state had unlimited resources, it could equalize across the entire wealth range. With a limit on spending, however, the state has two choices: 1) It can equalize across as much of the wealth range as its resources allow. 2) It may take from the poorer districts to provide aid to the additional districts. S.B. 4 produced a distribution similar to the equalized line. The compromise line is similar to the Foundation School Program distribution under H.B. 72. H.B. 72 provides some additional equalization aid which gives a flat, equalized distribution of aid over a small portion of the range. See Figure III-6. The effects of H.B. 72, S.B. 4, and the State Board's version of the old school finance system appear in Tables V-2, V-3, and V-4. By the author.

The third method is to determine how much the state is able to spend, and see how far it will go when local capacity is balanced exactly, as shown in Figure IV-2. In this case, the accountable cost is irrelevant, since the amount of the adjusted allotment is determined, not by real costs, but by the state's willingness to support the program. This process may result in overspending, but it is more likely to result in inadequate spending if there are other pressing claims on the state's revenues, since there is no attempt to determine the basic cost of education.

It should be obvious that the first method is preferable and that the others are compromises of that method. The first method complies with Article 7, Sec. 1 of the Texas Constitution because it ensures that all Texas school children will have a basic education. The other methods do not. Second, it ensures that the state's education spending will go to the areas of greatest need. Finally, it is a straightforward, defensible procedure. It would ensure that the districts without adequate revenue capacity could afford to provide the basic education, but would not do great violence to the current convention of allowing districts to utilize their excess revenue capacity.

DETERMINING THE LOCAL SHARE

The term "local share" refers to two very different things. The *local share of the Foundation School Program* is the amount calculated in order to determine the amount of state aid a district is entitled to. The proper term for this version of the local share is the "local fund assignment." The *true local share* is the real portion of a district's total spending that the district provides from its own resources. The state share of the Foundation School Program covered about one-half the average cost of maintenance and operations per pupil in 1984. The remaining portion, as well as the Local Fund Assignment, make up the true local share. This is illustrated by Figure III-2.

The Gilmer-Aikin Committee in 1949, recommended that the local fund assignment be 20-25 percent of the Foundation Program. By 1984, the Local Fund Assignment was 11.5 percent,[16] but the true local share of total school spending was about 50 percent.[17] There are two reasons for this. First, the legislature had reduced the local fund assignment several times. Second, the size of the Foundation School Program had not increased as quickly as school costs, so the FSP became a small part of total school funding. As a result of the state's unwillingness to fund the

program adequately, districts and local taxpayers were forced to bear an increasingly greater share of the burden. Simultaneously, the equalizing tendency of the Foundation Program was reduced.

The following example illustrates the concept of the true local share. If a district spent $2,700 per pupil from all sources in 1983-84 and the state and federal governments provided $1,600, the true local share was $1,100 or 40 percent of maintenance and operation.[18] If debt service is included, an average district's true local share of total school costs was 51 percent. The Foundation School Program included both the state share and the Local Fund Assignment. The FSP accounted for about $1,500 or 55 percent of the maintenance and operations and 45 percent if debt service is included.[19]

These figures have two implications. First, the Foundation Program was too small -- only 55 percent of operations costs and 45 percent of total costs. It did not represent the level of education that the majority of Texas communities considered necessary, so districts were forced to "enrich" to provide an adequate education. Second, the

tax effort that most communities were willing to make was greater than the effort required to raise the Local Fund Assignment of the Foundation Program.

The Local Fund Assignment of the Foundation Program has been a continuing controversy. Advocates for local property tax relief push to reduce the Local Fund Assignment in the mistaken belief that this will ease local tax pressures. When the size of the Foundation Program decreases relative to true costs, however, local property taxes must increase to cover the balance needed to provide an adequate education regardless of the LFA. Lowering the local fund assignment means that state aid is distributed more widely and, if total state expenditures are not increased proportionately, the basic Foundation School Program amount must be reduced. Either effort reduces the equalizing effect of the program. Further, less affluent districts cannot cover the balance without greatly increasing taxes on their inadequate tax bases. Therefore, reducing the Local Fund Assignment is less effective than increasing the Foundation School Program for reducing local property taxes.

The conclusion to be drawn here is that the local fund assignment should reflect the tax effort that districts

actually make. If local property tax relief is a worthy goal, it should be accomplished not by reducing the local fund assignment, but by increasing the size and scope of the Foundation School Program. For example, in 1983-84, the local fund assignment was 11 cents per $100 valuation. On the average tax base, that tax produced about $200. State aid provided about $1,300. The federal government provided about $300. The district raised the Local Fund Assignment of about $200 *and the balance of its needs for a total true local share of about $1,100.* The average tax rate for maintenance and operations was 58 cents in that period. Had the Local Fund Assignment been set at 50 cents per $100 valuation, the local fund assignment for the average district would have been about $900, which is less than the district's actual local revenues. If the Foundation Program allotment had been $2,400, reflecting the average cost of education minus the federal contribution for this average district, state aid would have increased to about $1,500 from $1,300. State aid would have displaced about $200 in local taxes per pupil, or the average district would have had $200 more per pupil to spend for education. That additional $200 per pupil represents increased state spending and, therefore, state taxes.

PERCENTAGE V. TAX RATE LOCAL FUND ASSIGNMENT

From 1950 to 1984, Texas based the Local Fund Assignment on a tax rate applied to each district's tax base. House Bill 72 made the LFA a varying percentage of the Foundation School Program allotment. In one sense, these two techniques are merely two sides of the same coin. The percentage LFA determines a tax rate, and the tax rate LFA determines the percentage. There are political and practical reasons, however, for choosing one or the other. The tax rate LFA has no permanence when local property values are in a state of change. The state/local share fluctuates widely, as the examples cited have shown. Since the state/local share ratio determines both the efficiency and equalizing effects of the state aid system, this fluctuation in the ratio makes the system unpredictable. The percentage LFA accurately reflects the state/local share ratio as property values change. The state/local ratio implies a tax rate. The implied rate of H.B. 72 was 27 cents per $100 valuation for the average district.

The tax rate LFA seems easy to talk about and to understand. Unfortunately, it is also easy to misunderstand. The most common misunderstanding is that it is a state mandated tax rate. Since H.B. 72 does not require a

district to raise its LFA, that contention is clearly false. The basic principles of the normative model require that the LFA be mandated, but at this time it is not. Because of this common misconception, the legislature is under pressure to lower the LFA, and it has done so in every session since 1975. (See Chapter II.) The consequences of lowering the LFA are less efficiency, less equalization, greater cost to the state, and, potentially, higher local tax rates. (See Chapter III.) The common misunderstanding and political abuse of the tax rate LFA, as well as the fact that all this tends to drive the LFA downward, argue for the percentage LFA.

CLASSROOM CONSTRUCTION AID

There are two justifications for classroom construction aid. First, H.B. 72 mandates lower class sizes. Therefore, it mandates that districts provide more classrooms. There is, however, no systematic effort to assess the impact of this mandate on school districts, nor does the state provide any aid to offset the local economic impact of the mandate. Second, districts with small tax bases are forced to pay for classroom construction by reducing maintenance and operation tax rates. Although it is not techni-

cally accurate, it is essentially accurate to say that poor districts must pay for classrooms with money that they otherwise would use for maintenance and operations. Therefore, classroom construction aid would have a positive impact on current operating costs. This report has shown that a realistic Foundation School Program --one which accounts for all of the requirements of a quality education -- will produce efficiency and equity. Classroom construction is part of the basic cost of education. Therefore, it should be included in the state aid system. The program is called *classroom* construction aid here, because a program which targets classrooms addresses the real concern that state aid should be used only to remedy the most pressing and relevant education need, not to provide extraneous facilities.

Classroom construction aid should not be included in the maintenance and operations portion of the Foundation School Program. Maintenance and operations funds pay for ongoing expenses, but any district's classroom needs depend on its existing facilities and pupil population growth, and construction is a one-time expenditure for any particular unit of need. Therefore, classroom construction aid should be a separate program with the following components:

1) *Classroom Construction Cost Assessment*

The state would conduct an ongoing assessment of classroom construction costs to develop realistic figures for the cost per classroom of the several options available for new classrooms: temporary structures, expansion or renovation of existing facilities, and new facilities of various types. These figures would be analogous to the Foundation School Program allotment per pupil.

2) *Need Assessment, Application, and Approval*

Eligibility would depend on an application and approval process to confirm the need of a district for additional classrooms and the options that are appropriate for the district -- temporary classrooms, new, permanent classrooms, or renovation of existing facilities.

3) *Equalized classroom construction aid*

The amount of classroom construction aid per classroom unit would depend on the wealth of the district, and would vary from 100 percent to none, just as state aid in the Foundation School Program varies.

SUPPLEMENTAL EQUALIZATION AID

In a perfect world, additional equalization aid would be unnecessary; the adequate FSP and fair local share would balance local revenue capacity perfectly so that poor school districts would be able to provide adequate educations. Unfortunately, there is no assurance that those necessary conditions will be met at all times, even with the best efforts of the state. And the state's best efforts have been inadequate in the past. Equalization aid would protect helpless school districts from such contingencies.

EVALUATION OF THE MODEL

The normative model presented above has two principal deficiencies which become clear when the model is compared to the following basic principles:

> *The adequacy and appropriateness of education cannot depend on local economic factors.*
>
> *The adequacy and appropriateness of education should not depend on the willingness of the voters in the local school district to support taxes.*

The first deficiency is that the model would continue to allow districts to underfund education. The

remedy would be for the state to require districts to levy the tax rate needed to raise their Local Fund Assignments. Politically, such a requirement does not seem advisable. The second problem with the model is that it would allow *budget balanced* districts -- those which do not receive state aid under the Foundation School Program -- to enrich above the level of the schools which receive state aid. Any district which is willing to have a higher-than-average tax rate would be capable of providing additional program, and the wealthier districts would be more capable of doing so than the poorer districts.

There are several possible solutions to this problem. The state could limit the tax rate of school districts. This would place all pupils on equal footing, but it would not solve the enrichment problem. For example, if the 1985 average tax rate were established as the limit, there would continue to be districts with large revenue capacity which would be able to provide generous programs, lower tax rates, or both.

The state could "capture" excess revenue capacity by requiring districts which produce an excess at the average tax rate to contribute their excess to the state educa-

tion fund. This method is used in California.[20] It does not seem likely that such a "Robin Hood" plan would be politically feasible in Texas.

The state could reinstitute the state ad valorem education tax, and deny school districts the authority to levy taxes. In this case, the proceeds of the tax would go directly to the state education fund. This approach is similar to H.B. 33 introduced by Representative Vowell in the 1984 Special Session.[21] It differs from H.B. 33 in that districts would not have the authority to levy any tax, whereas H.B. 33 would have allowed them to continue to do so. A state ad valorem tax would have the advantage of capturing the now unused revenue capacity of the wealthier districts. Analysis of H.B. 33 indicated that a tax rate of 45 cents per $100 valuation would have produced the same total revenue as the average rate of 58 cents per $100 valuation produced in 1984.[22] The plan would establish horizontal equity in property taxation for schools, and would eliminate the problem of equalization. It would lower the property tax rates of the majority of Texans. The plan is in compliance with the principle that the adequacy of education should not depend on the willingness of the voters in any particular district to support taxes. Finally, it

would allow the state systematically to decrease its reliance on the local property tax, since the property tax would be only one of the mix of taxes available to the state to fund education.

The first major objection to the Vowell plan is that it would allow no local control over revenues. Any disagreements about the adequacy of educational funding would have to be resolved in Austin. Local districts would have no recourse if the state did not provide adequate funding. This argument has only superficial validity. Only the wealthier schools in the state now have any significant control over their revenues. The poorer schools certainly do not benefit from their privilege of exercising local control over inadequate revenue bases. For the majority of Texas schools, state school funding levels determine the adequacy of education they can provide. The decision is made in the statehouse even now. Local control is more an emotional issue than a rational one. Districts have little choice over the quality of teachers they hire, staffing patterns, curriculum, or teacher pay. Their lack of control is due to long-standing state regulations and lack of adequate revenue capacity. In other words, only the wealthy schools have real local control over revenue, and they lack

control over the other major portion of their school operations. Nonetheless, the local control is such an emotionally charged issue that it alone will probably prevent adoption of a statewide ad valorem plan.

The second major objection to H.B. 33 relates to the effects of the loss -- real or imagined -- of local control. Support for public schools in Texas comes from a broad range of economic groups. In this state, the wealthy do not automatically send their children to private schools. Full state funding might remove the last control that wealthy schools and wealthy parents have over their school, the option of funding the school lavishly and treating it as if it were a private school. The equitable system of school finance described in this report would not prevent that, but full state funding would.

Within the limits of the possible, the normative model achieves a high degree of equalization, and does not vary radically from current practice. Being an incremental approach, it is more likely to be politically feasible than plans which eliminate local taxing authority.

Endnotes

Chapter IV

1. Governor's Committee on Public School Education, The Challenge and the Chance (Austin: 1968), pp. 17, 19.

2. Texas, Constitution, Art.7, Sec. 1.

3. Ibid.

4. Ibid., Art. 1, Sec. 3.

5. Vernon's Texas Codes Annotated, Education Code, Section 16.001.

6. Texas, Constitution, Art. 1, Sec.3.

7. John Rawls, A Theory of Justice (Cambridge, Mass.: The Belknap Press of Harvard University Press, 1971), p. 250.

8. Ibid., p. 100.

9. State Property Tax Board, "Property Value Category Analysis II -- 1982" (Austin: State Property Tax Board, August 12, 1983)

10. Roe L. Johns and Edgar L. Morphet, "Developing the Foundation Program" in Perspectives on the Economics of Education, ed. Charles S. Benson (Boston: Houghton Mifflin Company, 1963), pp. 325-329.

11. Texas, Constitution, Art. 7, Sec. 3.

12. Select Committee on Public Education (SCR 22), Construction, Rehabilitation and Repair, and Capital Debt Financing, report and recommendations submitted to the 68th Legislature (Austin: Select Committee on Public Education, November, 1982), p. 10.

13. Craig Foster, Executive Director, The Public School Resource Equity Center, Austin. Interview, Dec. 4, 1984.

14. Statement by Dr. Kent McGuire of the Education Commission of the States, before the Price Differential Index Committee, Austin, August 24, 1984.

15. Richard Hooker, Professor of Education, University of Houston. Interview, Austin, November 8, 1984.

16. Legislative Budget Board, Fiscal Size Up, Texas State Services, 1984-85 Biennium (Austin: Legislative Budget Board, 1984), p. 49.

17. Texas Research League, Benchmarks for 1984-85 School District Budgets in Texas (Austin: Texas Research League, 1984), Table 1, p. 2.

18. Ibid., Table 1, p.2; Table 11, p. 16.

19. Ibid.

20. James L. Phelps and Michael F. Addonizio, "District Power Equalizing: Cure-all of Prescription?" Journal of Education Finance 7 (Summer, 1981): 71-73.

21. House Bill 33 , by Jack Vowell, submitted to the 68th Legislature (Austin: Legislative Council, 1984)

22. Author's calculation from: State Property Tax Board, Annual Report for Tax Year 1983 (Austin: State Property Tax Board, 1984), p. 15.

Chapter V

CRITIQUE OF HOUSE BILL 72

The purpose of this chapter is to familiarize the reader with House Bill 72, the education reform measure passed by the 68th Legislature in the Special Session of 1984, and to critique the bill in light of the normative model presented in Chapter IV.

House Bill 72 is a complex bill which deals with many education issues besides finance. Some of these issues have a bearing on school finance in that they mandate changes in school operations. For example, the bill includes a lower pupil-teacher ratio, higher teacher salaries, special tutoring for certain pupils, and a number of other things which increase school costs. This report does not address the issues which have indirect effects on school costs. The purpose here is to critique the adequacy of the direct finance provisions of H.B. 72 in achieving equivalent levels of school funding in all Texas schools regardless of local property wealth.

DESCRIPTION OF THE FINANCE STRUCTURE OF H.B. 72

The finance provisions of H.B. 72 differ considerably from the finance system the bill replaced. Table II-1 allows comparison between the two systems.

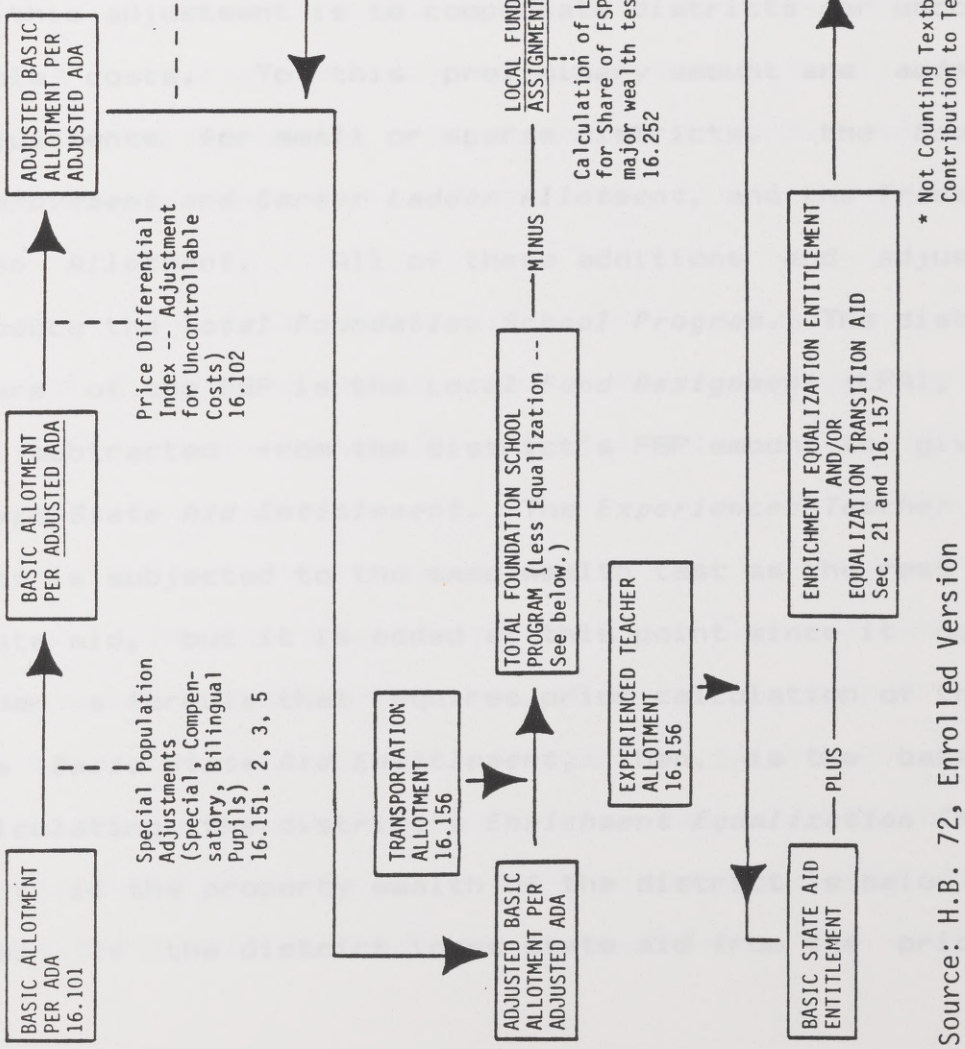
THE FOUNDATION SCHOOL PROGRAM

H.B. 72 is a unit cost system in which the unit is the pupil in average daily attendance. The system arrives at a basic cost figure for each school district which is the Foundation School Program size for that particular district. Then, a formula determines the district's share of that cost. In practice the system is more complicated. The actual procedure is illustrated by Table V-1. The greater part of the program are *in-formula* funds. That is, they are distributed according to an equalizing formula. They are wealth-tested. The Foundation School Program is *in-formula*. Unequalized funds are distributed to districts without regard to their ability to pay. These are textbook aid and the state contribution to teacher retirement.

In H.B. 72, the Foundation School Program size is based on a *basic allotment* of $1,290 per pupil in Average

Table V-1

The Finance Structure of H.B. 72



Source: H.B. 72, Enrolled Version

Daily Attendance (ADA) in 1984-85 and $1,350 thereafter. The average daily attendance of a district is adjusted upward to reflect the extra costs associated with special pupil populations. These adjustments include vocational, compensatory, bilingual, handicapped, homebound, and other special students. The *basic allotment per adjusted ADA* is adjusted again by the *price differential index* to produce the *adjusted basic allotment per adjusted ADA.* The purpose of this adjustment is to compensate districts for uncontrollable costs. To this preliminary amount are added any adjustments for small or sparse districts, the *Education Improvement and Career Ladder Allotment*, and the *Transportation Allotment.* All of these additions and adjustments produce the *Total Foundation School Program.* The district's share of the FSP is the *Local Fund Assignment* (LFA), which is subtracted from the district's FSP amount to give the *Basic State Aid Entitlement.* The *Experienced Teacher Allotment* is subjected to the same wealth test as the rest of the state aid, but it is added at this point since it operates under a formula that requires prior calculation of the LFA. The *Basic State Aid Entitlement*, then, is the basis for calculating the district's *Enrichment Equalization Entitlement* if the property wealth of the district is below average. If the district loses state aid from the prior aid

system, it is entitled, also, to *Equalization Transition Aid* through 1986-87. What the system accomplishes is this:

The *basic allotment* is a starting point that represents the basic cost of educating the typical pupil with no unusual educational needs in a district with no unusual cost factors. This number is adjusted upward to account for unusual circumstances and special pupil populations.

Special population adjustments recognize that a unit of education for special pupils is more expensive than an equivalent unit for regular pupils.

The *price differential index* is the adjustment for special district circumstances. Its primary purpose is to allow districts in highly competitive labor markets to pay competitive salaries.

The Education Improvement and Career Ladder Allotment is not much more than an add-on to the *basic allotment*. It seems that it had symbolic value in gaining the support of teacher groups during the Special Session. What it means is that the starting point for the adjusted basic allotment is $1,390 for 1984-85 instead of $1,290.

The finance system prior to H.B. 72 was based on a unit cost of *personnel units* -- teachers -- instead of pupils. The system was intended to made a district's hiring decisions neutral as to whether to hire an experienced or an inexperienced teacher. It was feared that the pupil unit system would penalize experienced teachers unless an incentive were added to hire or retain them. The purpose of the *Experienced Teacher Allotment* is to make district hiring procedures neutral regarding a teacher's experience.

The *Enrichment Equalization Allotment* provides an additional grant to districts with below-average (below 110 percent of average) tax capacity. This grant helps to compensate for the fact that poor districts cannot provide any significant amount of program enrichment because of their inadequate tax bases. As this report has pointed out, the need for enrichment equalization arises when the FSP is not large enough to cover the basic costs of education. One of the main deficiencies is that classroom construction aid is not part of the FSP. Enrichment equalization aid is a surrogate for classroom construction aid since it helps compensate poor districts with inadequate resources for the large effort they must make to provide classrooms. For this reason, H.B. 72 allows the enrichment equalization formula

to be based on the district's maintenance and operations tax rate combined with its debt service rate.

The figure that results from all this adjustment is the Foundation School Program amount for any particular school district. Whether the basic allotment and the adjustments that produce the Foundation School Program amount are adequate to provide a basic quality education is the subject of a later discussion in this chapter. For the program to be effective, the amount should be close to the actual cost of poviding a basic quality education for the particular children that make up a particular district. The actual amount of state aid that the district will receive is determined by the *local fund assignment*. A district of average wealth is responsible for 30 percent of its Foundation School Program amount (33 percent after 1984-85). The percentage will be lower for a district with less property wealth, and higher for a wealthier district. A district with 330 percent or more of the statewide average wealth per pupil will have a 100 percent LFA in 1984-85. Thereafter, districts with 300 percent or more of the statewide average wealth will have a 100 percent LFA.

The fact that a district has a 100 percent local

fund assignment does not mean that it will receive no state aid. It means only that it will receive no aid within the Foundation School Program distribution. Wealthy districts will continue to receive state aid through the teacher retirement system and textbook aid. These are unequalized entitlements. The *Equalization Transition Fund* is a temporary measure which provides additional aid to wealthy districts, regardless of need. It is supposed to be phased out by September 1, 1987. This measure is equivalent to the hold-harmless provisions in the previous education finance statutes. The transition fund is a part of the Foundation Program formulas. The other grants are unequalized aid.

UNEQUALIZED STATE AID

The state pays the employer's share of *teacher retirement*. The amount that the state contributes for any individual teacher depends on that teacher's salary. Since the teachers employed by wealthier districts tend to receive higher salaries, and since the employer's retirement contribution is a perquisite that helps attract personnel, the state's policy of assuming full responsibility for the employer's share of retirement contribution helps wealthy districts hire and keep more experienced personnel than poor districts. The state's contribution to the teacher retire-

ment system was $492 million in 1981-82.[1]

The state purchases and maintains ownership of textbooks. It distributes the textbooks to districts according to pupil populations and categories. In 1983, the State spent $51 million on this form of aid.[2] There is no wealth test in the provision of textbooks; districts receive the books free, regardless of ability to pay.

EVALUATION OF THE FINANCE STRUCTURE OF H.B. 72

Preliminary analysis of H.B. 72 indicated that it achieved improvements in the equity of school finance. The question is not whether the state should return to the pre-existing system, but whether H.B. 72 went far enough in correcting the injustices of school finance in Texas.

The normative model provides three basic questions to ask of H.B. 72: a) Is the *Foundation School Program* created by H.B. 72 adequate in size and scope? A subsidiary question is, does H.B. 72 include an adequate

system for assessing the costs of education and incorporating the results in the basic allotment? b) Is the *local fund assignment* adequate to provide an equitable and economical distribution of state aid? c) Does there continue to be *unequalized state aid* which compromises the efficiency and equalizing tendencies of the state aid system?

Since quantitative analysis of a subject as complex as school finance requires an enormous, up-to-date data base, a large computer, and considerable programming and computer time, the quantitative comparison of H.B. 72 in relation to the normative model will rely on analyses done by the Texas Education Agency for Senate Bill 4, introduced in the Special Session of 1984. S.B. 4 is in substantial compliance with the Local Fund Assignment requirement of the normative model. S.B. 4 does not, however, include textbook aid, the state's contribution to teacher retirement, or classroom construction aid in the Foundation School Program. Therefore, S.B. 4 is of smaller scope and size than the normative model. The results of S.B. 4 are sufficiently different from those of H.b. 72 and the prior system to demonstrate the effectiveness of the approach of the normative model.

THE ADEQUACY OF THE FOUNDATION SCHOOL PROGRAM IN H.B. 72

There are two measures for the adequacy of the FSP -- scope and size. The scope of the program refers to the aspects of school finance included in it. The scope of the program influences its size, but there are aspects of the scope of the program which deserve separate treatment because they influence the efficiency of the system of state aid. Chapter III demonstrated that the size of the FSP is critical to its ability to provide adequate equalization.

SCOPE

The Foundation School Program of H.B. 72 does not include textbooks, teacher retirement, or classroom construction. The provision of textbooks is equivalent to a per capita grant similar to the Available School Fund. This creates an equity problem since wealthy districts receive free textbooks regardless of their ability to share the purchase cost with the state. For the state to pay all of the employer's portion of teacher retirement creates the same efficiency and equity problems. The problem is magnified by the fact that wealthy schools have been able to pay larger salaries, so their teachers receive more state money on retirement than the lower-paid teachers of the poorer districts. The result is that the state subsidizes a por-

tion of the wealthy districts' decision to pay higher salaries. The state subsidizes the wealthy districts' larger benefits. This is not an argument against retired teachers receiving their due. It is justification for including teacher retirement within the Foundation formulas so that wealthy districts begin to pay a portion of the retirement contribution, commensurate with their ability to pay.

Classroom construction is a different problem. The state provides no direct aid for classroom construction. As Chapter IV explained, this means that no equity exists in the provision of school facilities. The taxpayers in poor districts must pay higher taxes for debt service, or the students of poor districts must go to school in inadequate facilities, or both. *Given that the state grant of revenue capacity to school districts is unequal*, the state has created the inequities. Inclusion of equalized classroom construction aid in the state aid program would redress the inequities.

SIZE

The S.C.O.P.E. committee recommended, originally, that the basic allotment of the FSP should be $1,850, 43 percent larger than the basic allotment in H.B. 72. The committee recommended that special population adjustments

for compensatory and bilingual education be 0.3, 50 percent and 200 percent higher, respectively, than the same adjustments in H.B. 72. An adjustment of 0.3 means that a special pupil counts as 1.3 regular pupils. The size of the committee's recommendations was reduced to produce Senate Bill 4.[3] The basic allotment was reduced to $1,715 from $1,850. The other factors remained virtually the same. The cost of S.B. 4 over current law was estimated at $837 million for 1984-85.[4] The cost of H.B. 72 was estimated at $848 million,[5] and the State Board of Education Plan, $911 million.[6] Although they are not strictly comparable, these amounts indicate that S.B. 4 would not have been more expensive than the other plans, despite its larger allotments and adjustments.

As this report has demonstrated, the size of the Foundation School Program entitlement has important effects on equalization and local taxes. The larger allotment and adjustment sizes make the school finance program more equitable and reduces the tax burden on local taxpayers in most districts. To the extent that the size of the Foundation School Program allotments are lower than the real costs which school districts must bear to provide a basic, quality education, the program fails to equalize and forces local

taxpayers to bear a higher burden.

THE SYSTEM FOR ESTIMATING TRUE COSTS FOR THE BASIC ALLOTMENT

H.B. 72 requires the State Board of Education (S.B.O.E.) to report biennially to the legislature on the annual average accountable costs of a quality education.[7] The bill requires the legislature, however, merely to "consider the recommendations." in setting the size of the basic allotment and the adjustments to it.[8] This soft language allows the legislature to ignore the recommendations with the result that education might be underfunded in the future. The Price Differential Index, however, "shall be adopted."[9] Adoption of the PDI is the responsibility of the S.B.O.E., not the legislature. The different treatment of the Index may be traced to the maintenance of legislative prerogative. The PDI, however, will have a profound effect on the cost of public school finance to the state. That is to say, the Index can have an undue effect on the appropriation system. Yet, the PDI is less critical to adequate school funding than adoption of an adequate accountable cost figure. As Chapters III and IV argued, accurate estimation of the true costs of education is fundamental to an adequate education funding system. *The failure to provide for firm acknowledgement of the accountable costs of education is the*

single greatest failure of H.B. 72.

THE ADEQUACY OF THE LFA IN H.B.72

The S.C.O.P.E. committee recommended a local fund assignment of 40 percent of the Foundation School Program amount of the average school district. H.B. 72 uses a LFA of 30 percent for 1984-85 and 33 percent thereafter. This report has shown that the smaller local fund assignment means a less efficient distribution of state aid and less equalization of school funding. See Chapters III and IV.

A factor in any consideration of the adequacy of the LFA in H.B. 72 is the optional nature of the LFA. The law does not require any district to raise its LFA. The normative model stipulated that the education that pupils in any district receive should not be dependent on the willingness of the taxpayers in their district to support taxes. Unless the LFA is mandatory there is no guarantee that the pupils of any district will receive an adequate education.

UNEQUALIZED STATE AID IN H.B. 72

H.B. 72 retains the three forms of unequalized state aid already discussed under "SCOPE": unequalized

state grants of tax capacity for construction, textbooks, and the teacher retirement contribution. The last two items alone represent approximately $550 million for 1984-85 distributed without regard to need. Textbook purchases cost $51 million[10]; Teacher Retirement cost $492 million in 1981-82.[11] To the extent that these funds go to school districts which have the revenue capacity to raise these amounts with a tax rate at or below the average, the state aid system remains inefficient, tax burdens remain unequal, and school funding remains inequitable.

THE RESULTS OF H.B. 72

Table V-2 shows the effect of H.B. 72 on different wealth groupings. Column 1 shows total state aid per pupil, not counting textbooks or state contributions to teacher retirement. Column 2 shows each wealth group's state aid as a percentage of the average aid. Both of these columns indicate that state aid increases as the wealth of the district decreases, but the percentages in Column 2 allow comparison of this table with Tables V-3 and V-4. The gross amounts are misleading for purposes of comparison, and tend to obscure the critical issue -- whether one plan achieves a more equitable distribution of state aid than another. Column 3 shows total funding per pupil from both state and

local sources assuming an average tax rate of 58 cents per $100 valuation, and not counting textbooks, state contributions to teacher retirement, or local taxes to retire debt. Column 4 shows each group's total state and local revenues as a percentage of the average total revenues. Again, this is the column to use when comparing the effects of H.B. 72 with the other plans. Total revenue is the proper gauge of the equity of any finance plan since it accounts for the state grant of tax capacity. When total revenue is taken into account, the poorer and average districts are shown to be in a less favorable position than wealthier districts even though more state aid flows to the less affluent districts.

Tables V-3 and V-4 show the effects of the State Board of Education plan and Senate Bill 4, both of which were presented to the legislature during the Special Session of 1984. Columns 2 and 4 in the tables allow comparison between the three plans. The S.B.O.E. plan would have produced the largest difference between rich and poor districts, with the poor districts the losers. Under the S.B.O.E. plan the poorest districts would have had 80 percent of the average revenue, while the wealthiest districts would have had 175 percent of the average. S.B. 4 would have produced a distribution of total resources superior to

both the S.B.O.E. plan and H.B. 72. Under S.B. 4, the poorest districts would have had revenues equal to the average, while the wealthiest districts would have had 157 percent of the average. The middle group in the tables would have had 91 percent of the average under the S.B.O.E. plan and 93 percent under S.B. 4. Under H.B. 72, the poorest group would have had 89 percent of the average total revenue, the middle group would have had 90 percent, and the wealthiest group 172 percent. These figures show that H.B. 72 is inferior to S.B.4, but represents an improvement in equity over the previous school finance system as represented by the S.B.O.E. plan. The school finance system represented by S.B. 4 does not include textbook aid, the state contribution to teacher retirement, or classroom construction aid. As this report has shown, the effectiveness of the Foundation School Program, as well as the number of districts included in its aid distribution, hinges on size and scope of the program. This report has provided a conceptual framework which indicates that inclusion of those additional forms of aid in the FSP would result in a state aid program superior to both S.B. 4 and H.B. 72.

Table V-2

The Effects of H.B. 72 by Wealth Groups

WEALTH (Market Value $ per ADA)	1 State Aid per Pupil	2 State Aid as a Percentage of Average	3 Total State and Local Revenues	4 Total Rev. as a Percentage of of Average
Under 83,000	$2,194.2	141%	$2,521.9	89%
83,000-107,999	2,028.2	130%	2,582.1	91%
108,000-134,999	1,930.2	124%	2,634.9	93%
135,000-176,999	1,652.3	106%	2,557.1	90%
177,000-241,000	1,442.9	93%	2,657.9	94%
242,000-430,999	1,129.4	73%	3,081.9	109%
431,000 or Over	726.0	47%	4,875.9	172%
Average 220,209	1,555.6	100%	2,832.8	100%

Calculation of total state and local revenue uses the median of each wealth range and a tax rate of 58 cents per $100 valuation. For the poorest wealth range the low figure used was $30,000, for a median of $56,500. For the wealthiest range, the high figure used was $1,000,000. The true high figure is $14,000,000, but the highest-wealth districts are excluded arbitrarily as unrepresentative.

Source: "Fiscal Impact Model, H.B. 72, Conference Committee Report,"(Austin: Texas Education Agency, June 28, 1984), p. 2.

Table V-3

The Effects of the State Board of Education Plan By Wealth Groups

Wealth (Market Value $ per ADA	1 State Aid per Pupil	2 State Aid as a Percentage of Average	3 Total State and Local Revenues	4 Total Rev. as a Percentage of of Average
Under 83,000	2,060.8	125%	2,388.5	80%
83,000-107,999	2,084.1	126%	2,638.0	88%
108,000-134,999	1,983.3	120%	2,688.0	90%
135,000-176,999	1,829.4	111%	2,734.2	91%
177,000-241,999	1,600.8	97%	2,815.9	94%
242,000-430.999	1,336.3	81%	3,288.0	110%
431,000 or Over	1,075.3	65%	5,225.2	175%
Average 230,681	1,652.6	100%	2,990.5	100%

Calculation of total state and local revenue uses the median of each wealth range and a tax rate of 58 cents per $100 valuation. For the poorest wealth range the low figure used was $30,000, for a median of $56,500. For the wealthiest range, the high figure used was $1,000,000. The true high figure is $14,000,000, but the highest-wealth districts are excluded arbitrarily as unrepresentative.

Source: "Fiscal Impact Model, H.B. 72 -- Committee Amendments"(Austin: Texas Education Agency, June 18,1984), p. 2, column 7.

Table V-4

The Effects of Senate Bill 4 by Wealth Group

WEALTH (Market Value $ per ADA	1 State Aid per Pupil	2 State Aid as a Per- centage of	3 Total State and Local Revenues	4 Total Rev. as a Per- of Average
Under 83,000	$2,449.9	161%	$2,777.6	100%
83,000- 107,999	2134.9	140%	2,688.8	97%
108,000- 134,999	1,970.5	129%	2,675.2	96%
135,000- 176,999	1,685.3	111%	2,590.1	93%
177,000- 241,999	1,351.8	89%	2,566.9	92%
242,000- 430,999	927.6	61%	2,879.3	104%
431,000- or Over	219.5	14%	4,369.4	157%
Average 216,207	1,523.4	100%	2,777.0	100%

Calculation of total state and local revenue uses the median of each wealth range and a tax rate of 58 cents per $100 valuation. For the poorest wealth range the low figure used was $30,000, for a median of $56,500. For the wealthiest range, the high figure used was $1,000,000. The true high figure is $14,000,000, but the highest-wealth districts are excluded arbitrarily as unrepresentative.

Source: "Fiscal Impact Model -- S.B. 4 -- Article II with Subchapter B" (Austin:Texas Education Agency, June 8, 1984).

Endnotes

Chapter V

1. Teacher Retirement System, Annual Report for 1981-82 (Austin: The Teacher Retirement System, 1983).

2. Comptroller of Public Accounts, State of Texas 1983 Annual Financial Report (Austin: Comptroller of Public Accounts, 1984) Table 40, Group 02, p. 134.

3. Interview with Dr. Richard Hooker, Professor of Education, University of Houston. Austin: November 8, 1984.

* 4. Texas Education Agency, "Fiscal Impact Model, SB 4, Article II with Subchapter B" (Austin: Texas Education Agency, June 8, 1984): p. 1, column 8.

* 5. _____, "Fiscal Impact Model, H.B. 72, Conference Committee Report" (Austin: Texas Education Agency, June 28, 1984), p. 1, column 8.

* 6. _____, "Fiscal Impact Model, H.B. 72 -- Committee Amendments" (Austin: Texas Education Agency, June 18, 1984), p. 1, column 8.

7. Vernon's Texas Codes Annotated, Sec. 16.201.

8. Ibid., Sec. 16.203.

9. Ibid., Sec. 16.179.

10. Comptroller of Public Accounts, Ibid.

11. Teacher Retirement System, Ibid.

*Fiscal impact models are rarely published. The results of any particular model may vary from day to day since the Texas Education Agency updates its data base continually. Models of different proposals are strictly comparable only when done with the same data, on a "frozen" data base. The calculations used in Tables V-2. V-3, and V-4 allow comparison between one aspect of the models, their relative equalizing effects. The models are not comparable in terms of absolute dollar amounts.

Chapter VI

CONCLUSIONS AND RECOMMENDATIONS

This report has demonstrated that constitutional and statutory mandates, as well as the basic principles of justice, provide an effective standard by which to evaluate public school finance in Texas. The school finance system prior to H.B. 72 failed to comply with those standards but had moved toward and retreated from them periodically. H.B. 72 represents a significant improvement, but fails in several regards. This paper has dealt with the failings of the finance portion of H.B. 72, and has discussed a number of possible remedies. The recommendations which follow, however, are simple and of limited scope. The author does not believe that major changes in the school finance system are advisable at this time. For example, full state funding is the ultimate answer to the problems of equity between school districts and among property taxpayers. The political and practical obstacles, however, to such a radical change in the system seem too great, assuming that the change would be desirable.

SHORT STEPS TO EQUITABLE SCHOOL FINANCE

DO NOTHING

H.B. 72 created a new mix of winners and losers. The losers will be active in attempting to persuade the legislature to alter the system in their favor. It is likely, for example, that schools which are receiving Equalization Transition Aid will ask the legislature to make that provision permanent. It is scheduled now to end in 1987. This sort of extension was granted for the hold-harmless provisions of the previous finance system. The purpose of the provision is to protect school districts which would lose state aid or be forced to increase local taxes under the new finance system. The majority of such districts have over three times the average property wealth. That is, they can have either three times the average revenue at the average tax rate, or one-third the average tax rate at the average revenue, or some compromise of the two. To be blunt, the Equalization Transition Fund subsidizes low tax rates in wealthy districts.

The Equalization Transition Fund extension is only one example of the sort of measure that legislatures have faced following the passage of school finance reforms.[1] The safest course for the legislature is to have a morato-

rium on any changes until the latest reforms are well entrenched.

ENSURE THAT THE BASIC ALLOTMENT IS ADEQUATE

The major failure of H.B. 72 is that the bill did not establish a firm commitment to fund the program adequately. This report has shown that the size of the FSP relative to the true costs of education is critical to the operation of an effective school finance system. In the terminology of the Education Code, the critical amount is the Basic Allotment, since that figure is the major determinant of the size of the Foundation SChool Program. To the degree that the Basic Allotment is smaller than the actual costs which school districts bear, the state funding system will be inequitable and will force school districts to rely more heavily on local property taxes. H.B. 72 requires the Texas Education Agency to develop estimates of the accountable cost of the accredited education so the legislature can judge the adequacy of the basic allotment. T.E.A. has expressed reluctance to develop the estimates.[2] Sections 16.201, 16.202, and 16.203 of the Education Code should be amended to ensure that T.E.A. develops adequate reports on the accountable costs of the accredited program, and to ensure that future legislatures give adequate consideration

to those costs in making appropriations.

TIE THE LOCAL FUND ASSIGNMENT TO A REALISTIC LOCAL EFFORT

When the LFA is smaller than the average tax rate, the distribution of state aid is inefficient, since aid goes to school districts that have the ability to pay for their programs. Lower LFAs result in larger state obligations. An adequate LFA is a matter of efficiency and economy. Whether the average tax rate is appropriate as the LFA is open to question. Tying the LFA to the average tax rate could have unexpected effects which this report has not attempted to explore. The basic fact of the matter, however, is that the LFA should require close to the average tax rate.

ELIMINATE UNEQUALIZED STATE AID

Unequalized forms of state aid such as the textbook distribution system and the teacher retirement contribution are sources of inefficiency in the state's school finance system. Inclusion of these forms of aid in the Foundation School Program would save money and improve the equity of the system.

INCLUDE CLASSROOM CONSTRUCTION IN THE STATE AID SYSTEM

The legislature will probably face pressure during the Regular Session of 1985 to soften the pupil-teacher ratio or class size requirements imposed by H.B. 72. These pressures arise from the fact that reduced class size results in higher costs for school districts which are not already conforming to the new requirements. Average and poor districts are less likely to be in conformance with the mandate. The more stringent class size requirements are an example of a state regulation which results in higher costs for school districts, and especially for average and poor districts. As this report has demonstrated, a state aid system which fails to recognize the total, true costs which local school districts face is less effective, less efficient, and less equalizing. The state aid system under H.B. 72 attempts to provide an adequate amount of money for teacher salaries to pay for the increased number of teachers that the smaller class sizes will require. Unfortunately, smaller classes require more classrooms, as well as teachers. The problem goes beyond the temporary period of adjustment to the more stringent requirements; poor districts long have been forced to reduce current service levels in order to pay for capital construction. The program of classroom construction aid described in this report would help relieve both the temporary problem created by the new

requirements and the chronic problem faced by the state's poor districts. By encompassing a large portion of school costs, a classroom construction aid system would improve the equity of the total school finance system. This report has not attempted to estimate the cost of such a program to the state. The system described included a need assessment and the use of various options to reduce classroom construction costs. The implication should be made clear: classroom construction aid should be used to meet minimum, basic facility needs. With that restriction, the cost to the state should not be prohibitive. An additional benefit is that the state taxes required to fund the program would displace the local taxes that would otherwise be spent for this purpose.

CONCLUSION

Major reforms are almost always controversial. The education reforms of 1984 were more controversial than usual, perhaps due to the difficulty of understanding the results, and certainly because of the number of vested interests who insisted on disputing every facet of the proposals. My role during the Special Session was to analyze the proposals, to evaluate the analyses of the propos-

als provided by various agencies, and to advise a number of state representatives. During that time, I came to the conclusion that true reform of the state's school finance system could take place only if the mechanics of school finance were made understandable. Making school finance understandable was one goal of this report. The relative simplicity of H.B. 72 made the task easier. The finance system that preceeded H.B. 72 was considerably more complex. I doubt that I would have attempted to clarify that system. A major triumph of the Special Session was a school finance structure that legislators, laymen, and school personnel can understand. That means that the system will be easier to supervise and control. It is not surprising that some of the most vocal objections to the bill came from persons whose livelihoods depend on their exclusive knowledge of the workings of school finance in Texas.

This report has shown that the mechanics of the Foundation School Program are relatively simple, and that its broad effects are as predictable as gravity. The operative factors are the size of the adjusted FSP allotment relative to the true cost of education and the Local Fund Assignment relative to actual local revenues.

There are several dangers for efficient, equitable school finance in Texas. This report recommended that rather than retreat from the reforms of H.B. 72, the legislature would better serve the people of Texas by doing nothing to the fundamental structure of H.B. 72. That is the safest advice. The other recommendations would represent positive improvements, but opening the school finance issue is laden with danger. Any close observer of the Special Session of 1984 could see that trusted persons of authority, as well as special interests, sought both to cloud the finance reform issue and to mislead the legislature. It is a measure of the quality of leadership in the legislature that those attempts largely failed. The special interests which lost during the Special Session will be back.

All that could damage school finance in Texas, however, is not in education bills. There seems to be considerable dissatisfaction with the property tax reforms of 1979. As this report showed, uniform appraisal practices and 100 percent appraisal are essential to the operation of the Foundation School Program. Retreat from the property tax reforms would virtually destroy the school finance system by opening it to manipulation and subtrefuge, and consequently, to inefficiency and inequity.

H.B. 72 improved the fairness, the equity, and the justice of school finance in Texas. This report has argued that the bill did not go far enough. To overemphasize that is to ignore one of the great triumphs of the legislation -- it made it *possible* to go far enough.

Endnotes

Chapter VI

1. Susan Fuhrman, "The Politics and Process of School Finance Reform." Journal of Education Finance 4 (Fall, 1978): 158-178.

2. William Kirby, Deputy Commissioner for Finance, Texas Education Agency. Statement before the Legislative Education Board, November 8, 1984.

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